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PREFACE

THE lengthening shadow of the European war fell across the sessions of the Semi-Annual Meeting of the Academy of Political Science. Every speaker felt the compulsion of that fact. It influenced all the appraisals of recent attempts to break through the barriers of economic nationalism, and it placed an extraordinary restraint upon predictions concerning the future of international trade. Much depends on the outcome of the present conflict. If we must continue to live in a " mercantilist, nationalist bellicose world", we shall need to be uncommonly wise to determine how far our national commercial policy may deviate from protectionist principles. That is the problem realistically explored in this volume of the PROCEEDINGS, for it contains the papers and addresses and extemporaneous discussions of the Academy's conference at the Hotel Astor in New York City on April 11, 1940. Its pages might well be read, for purposes of illuminating comparison, in connection with the PROCEEDINGS for May 1932, which were devoted to "The Crisis in World Finance and Trade". Against that background the prospect of a freer international exchange of goods and services is not entirely obscured, even by the clouds of war.

The officers and members of the Academy are under deep obligation to the speakers whose formal papers or impromptu remarks contributed to the success of the Semi-Annual Meeting. The program and arrangements were admirably handled by the following committee: Nicholas Murray Butler (Chairman), Miss Ethel Warner (Director), Frank Altschul, W. Randolph Burgess, Frederic R. Coudert, F. Trubee Davison, Lewis W. Douglas, Leon Fraser, Pierre Jay, Thomas W. Lamont, Roswell C. McCrea, Charles Merz, Wesley C. Mitchell, Shepard Morgan, William L. Ransom, Ogden Reid, David Sarnoff, Whitney H. Shepardson, Eliot Wadsworth, Thomas J. Watson, John H. Williams, Leo Wolman.

CONTENTS

PART I

RECIPROCAL TRADE AGREEMENTS: POLICY, PRACTICE AND PURPOSES

INTRODUCTION *

WESLEY C. MITCHELL, *Presiding*
Professor of Economics, Columbia University
Director, National Bureau of Economic Research
President of The Academy of Political Science

I HAVE the pleasure of opening the Semi-Annual Meeting of the Sixtieth Year of The Academy of Political Science.

On this occasion we are under particular time pressure inasmuch as a broadcast has been arranged for the remarks that are to be made at the luncheon. We all realize how tyrannically modern technological equipment controls our wishes and our actions; how imperative, for example, a telephone call seems. But the real triumph in imperious control over what we do has been attained by the radio. This little company is under an insistent moral compulsion to suit its convenience to the much larger, though shadowy, audience of the air, which has been informed that it can have its share in our pleasures at a specific time. We must, therefore, conform our proceedings to that requirement.

In the circumstances, the duties of the presiding officer, I think, should be no more than the duties of a timekeeper. I shall therefore dispense with remarks of my own upon the topic of the morning, "Reciprocal Trade Agreements: Policy, Practice and Purposes", and I shall also deprive myself of the pleasure of saying how grateful the Academy is to the distinguished speakers who are to address you. Fortunately introductions are unnecessary, for the speakers are widely known as leading authorities in their respective fields.

Let me then, with this brief statement, present our first speaker, Professor Joseph A. Schumpeter, of Harvard, who will discuss the influence of protective tariffs on the industrial development of the United States. Professor Schumpeter!

* Opening remarks at the First Session of the Semi-Annual Meeting.

THE INFLUENCE OF PROTECTIVE TARIFFS ON THE INDUSTRIAL DEVELOPMENT OF THE UNITED STATES

JOSEPH A. SCHUMPETER
Professor of Economics, Harvard University

I

I FEEL strongly that nothing but confusion and misunderstanding can result from any analysis of the effects of protective tariffs from purely economic considerations and without reference to the wider ambitions of the nation concerned and to the particular world situation into which its lot is cast. Hence I must devote time, which I sorely need for that purely economic aspect, to what I may term the political setting in which the practical question of protection always has presented, and is now presenting, itself to the people of this country.

First and last, what the American people wanted to accomplish, when they decided to stake their all on independence, was to be a world unto themselves, to work out their own destiny, to be rid of the vicissitudes of Europe and, most important of all, to be no longer pawns on the English chessboard; and this has, in the economic as well as in every other sphere, remained all along the only truly American foreign policy. I will say at once that this accounts for the fact that, though protection immediately creates protectionist interests that will clamor for additional protection for very obvious business reasons, the people at large, with an exception to be noticed presently, have given consistent support to a policy of protection and that they have all along refused to listen to what mere economists might have to say about it.

Attempts at protection, thwarted by the vetoes of colonial governors, were made even before the War of Independence. From the struggle for independence, the country emerged in a protectionist mood that asserted itself before long in the face of many anti-protectionist interests. Protection—or noninter-

course acts and so on—then was simply the economic complement of political independence or of the will to buttress that independence. Anti-protectionist interests, particularly those of wheat growers and cotton planters, were strong enough to put a brake on that fundamental tendency until the Civil War, and even succeeded in enforcing a strategic retreat of the protectionist high command from the " tariff of horrors "—the high-water mark of its success. But when, after the Civil War, it became clear that the immigration of European capital would for an indefinite time solve the problem that protection would otherwise have created, the protectionists had their way, with but minor setbacks, right up to the threshold of the World War. In the discussion of American post-war policy, especially of the Fordney-McCumber Act and of the famous " refusal to accept the implications of the country's new creditor position," it has been persistently overlooked, how much that policy of protection—as far as its popular support went—was part and parcel of the unequivocal verdict passed by the American people upon the Wilson policy, the League of Nations idea or anything that would perpetuate European entanglements. To be sure, it was illogical to embark at the same time upon a policy of forcing exports; but that was no more than a ransom paid to a restricted, if vocal, group.

This argument, however, does not apply to deviations from the principle of protection that aim at extending the country's economic sphere of influence on the continent of America, although such a policy may be the source of problems of a different kind. But barring that, the fundamental rationale of American protectionism is as strong today as it ever was. It may well gather additional strength in the near future.

It will be seen that what I have said so far is not likely to please the economist. In fact, it does not take account at all of the balance of purely economic advantage and disadvantage. Though the economic case for free, or less restricted, trade is not so strong and the economic case for protection not so weak as a bygone generation of economists believed, I do not wish to identify myself with any of the popular arguments that are being adduced for protection in general, or for certain types of protective measures in particular. I readily admit that they are, on the whole, much below the old free-trade argument.

I also admit that, if we lived in a peaceful world, the costs of the economic independence of this country might easily outweigh its advantage. But I submit that, since we do not live in a peaceful world, even the purely economic balance, both from the standpoint of industrial development and from the standpoint of the standard of life of the masses, may well be in favor of protection.

II

The industrial development of the United States, in the early stages of the growth of the industrial organism as a whole, as well as in the early stages of each individual industry, presents an almost ideal case for the application of the (Hamilton-List) infant-industry argument. There is no doubt a considerable list of instances—from watches to motor cars—in which industries either from the outset were, or very quickly became, so superior to any actual or potential foreign competition that nothing could have stopped, or even retarded, their success. But in the majority of instances, nascent American industries found foreign producers in possession. That the emergence of those industries and their conquest of the American market—also the development of certain factors, such as water power—were materially facilitated by protection is obvious.

It should be added that, in the American case, *some* of the most serious disadvantages that are usually associated with a policy of fostering industrial development in this way do not show at all, or do so in a much milder form than we should expect them to show in any other country. To begin with, the country soon grew so large as to make it possible to reap within its frontiers practically all the benefits that are usually attributed to a free-trade policy—benefits that are (like other things) now threatened by recent developments. If the restrictions that are now being placed on interstate and even interlocal commerce should continue to increase, more pressure on the people's standard of life may result than could ever be exerted by any amount of protection.

Moreover, protection usually overdevelops the protected industries, thus creating maladjustments for the future. The history of European protection abounds with instances of that. They are not entirely wanting in the history of this country. The depression following upon the peace of 1814 (just as

serious, proportions guarded, as the one following upon 1929) was characterized by the breakdown of many firms that owed their sickly life to the "protection" extended to them by the war, and conditions akin to war, with England. But on the whole, that phenomenon has been conspicuous by absence. The size and natural wealth of the country always absorbed whatever may have been due to the stimulus of protection, and little loss has been incurred *on that account.* To put it differently, protection did not lead to major distortions in the industrial structure. On the contrary, American protection on the whole resulted in a better balanced organism and in all-round, instead of one-sided, development.

That does not mean, of course, that losses of another kind were entirely avoided or that the protectionist policy was costless. A number of industries, of which wool and sugar are conspicuous instances, always remained, for a considerable part of their output, *dependent* on protection. It is those cases of "high-cost industries" which, though they demonstrate, still better than any other, the power of the tariff to increase the size of a country's industrial apparatus, are particularly exposed to well-founded objections on purely economic grounds. As a matter of general theory, it is indeed difficult to find any justification for the cost principle in tariff making, however strongly it may appeal to the untutored mind.[1] But in times like the present one, in which conditions of underutilization of resources prevail, there is reason to believe that, even in those cases and in the long run, a policy of protection does more good than harm, while it is clear that in the short run discontinuance of protection would create most serious difficulties of adjustment.

[1] There is, however, a purely economic argument for protection even in those cases. The differences between domestic and foreign costs that are to be equalized by tariffs are, of course, differences in terms of money. Now differences in money costs may be due either to differences in real costs—it may for instance take more man hours to produce a certain commodity in this country than it does to produce it abroad—or simply to the fact that money values all round are higher in this country than they are abroad. The theoretical argument referred to in the text fully applies to the first case only. In the latter case the tariff only prevents adjustment of values and in particular of money incomes to world-market standards. That may be desirable or not, but is in any case an entirely different matter—in fact, a question of the monetary policy to be pursued.

In *any* case, however, protection increases the rate of profit. Whatever we may think about this from other standpoints, in a rapidly progressing country it will have the effect of accelerating the pace of that progress by propelling investment and making it easier to face risks. After a state of maturity has been reached and especially in a prolonged period of depression such as the one that set in toward the end of 1929—whatever its causes and nature may be or have been—this argument would of course not apply. But obviously, in so far as protection reduces losses, keeps markets from being disorganized by foreign distress sales and so on, another argument takes its place. Also, independently of either booms or depressions, the fiscal interest in profit margins is an important consideration.

Taking this country's industrial organism as a whole, and with qualifications that should be obvious from what has been said above, we may thus conclude that, as far as the past is concerned, the main effect of protective tariffs has been to speed up industrial developments that would have come about in any case, rather than to induce developments that would never have come about without them. As far as this goes, their effect may well be likened to the effect of that kind of inflationism that has been characteristic of this nation from its origins to the present day. *Always*, and even during periods that are commonly dubbed deflationist, the American people were bent on monetary or credit expansion, and on "liberal" financing that did not look too closely at the purpose to be financed — from Franklin to Roosevelt that attitude has not changed except as to techniques and phraseology. And it must be admitted that, in the conditions of this country, our judgment on this practice cannot be quite what it would have to be in the case of any other country. As regards industrial development in particular, there cannot be any doubt but that it *was* accelerated beyond the rate that stricter practice would have allowed.

Of course, I do not mean to defend inflationism or, when it comes to that, the rate of industrial development itself. For instance, it is certain that the violence of American booms and breakdowns has partly been the consequence of loose finance and protection. It might well be argued that this country would today be a healthier and happier place, and that its problems would be much more manageable, if industrial prog-

ress had been less rapid and if there had been less of monetary expansion, of protection, of immigration. Our result, however, stands nevertheless. If size of industrial apparatus or amount of wealth is what we focus our attention on, then the effect of those three factors has been clearly positive — the country is now much richer than it would be without them.

But whereas, at the present stage of the country's economic evolution, there is *no* argument for further immigration, and whereas inflationary policies can henceforth have no function except that of palliatives in extreme cases of depression, the protectionist policy has not yet outlived its usefulness.

Even if there should never again arise a case in which protection could play the rôle it used to play in the past — and there is no warrant for assuming this—it will continue to be one of the simplest means of safeguarding the existing industrial structure. Given present conditions, situations will unavoidably arise in which temporary vicissitudes in other parts of the world might cause permanent damage to American industries. Of course these considerations exclude neither bargaining for advantages in individual cases (introduced, as a principle, in 1897) nor occasional resort to reciprocity agreements. But if we have got to live in a mercantilist, nationalist, bellicose world dominated by a few great empires, on the one hand, and if the domestic policy of this country is to remain free to shape its own destiny, on the other hand, I do not see the possibility, and I should very much doubt the wisdom, of any major deviation from the policy of protection.

Remarks by the Chairman

President Mitchell: Our second speaker is the Honorable Henry F. Grady, Assistant Secretary of State in charge of Trade Agreements, who will address us on " The Reciprocal Trade Agreements as an Evolution in Tariff Policy ". Mr. Grady!

THE RECIPROCAL TRADE AGREEMENTS AS AN EVOLUTION IN TARIFF POLICY

HENRY F. GRADY
Assistant Secretary of State

THE reciprocal trade agreements program of the United States is now approaching the end of its sixth year of existence. In this period of administration its basic characteristics and principles have become well defined and established. All of its essential elements are to be found in principles, methods and procedures which individually have characterized our tariff making at one time or another, and it may be of some interest to note the nonpartisan character of these precedents, in that they are to be found in legislation enacted under Republican as well as Democratic administrations.

In the combination of these elements into a balanced, coherent and rational tariff and commercial policy, however, as has been accomplished through the reciprocal trade agreements program, they have attained a new significance which reflects a new development in our national consciousness.

The trade agreements program was inaugurated in 1934 by an amendment to the Tariff Act of 1930, for an initial period of three years, and has twice been extended for similar periods. This amendment, known as the Trade Agreements Act, authorizes the President to enter into trade agreements with foreign governments with a view to obtaining improved market opportunities abroad for American products and pursuant thereto to proclaim modifications in our own rates of import duty, or other import restrictions, on foreign goods entering our markets. It provides, furthermore, that duties or restrictions proclaimed pursuant to such agreements shall apply to imports of the specified products, not only from the country with which the agreement is concluded, but also from all other countries which do not discriminate against American trade. It also requires that public notice shall be given of intention to negotiate a trade agreement in order that interested persons may have opportunity to present their views; and that, before con-

cluding trade agreements, information and advice shall be sought from the Tariff Commission, the Departments of State, Agriculture and Commerce, and from all other appropriate sources.

The foregoing sets forth very briefly the substance of the basic elements on which this program is founded. Each of them would in more complete presentation require qualification and amplification, but in the following we may see the six essential phases of this commercial policy, namely:

1. Reciprocity;
2. The most favored nation principle of equality of treatment;
3. Tariff bargaining procedure;
4. Delegation of authority by Congress;
5. Receipt and consideration of the views of private interests;
6. Formulation of proposals on the basis of expert research and analysis.

Reciprocity as a factor in tariff making consists in the granting of favorable or improved customs treatment of foreign products in return for similar treatment by foreign countries of domestic products. It was under the Republican tariff acts of 1890 and 1897 that the principle of reciprocity first appeared in our tariff history. Two different procedures were involved in these acts. With reference to a small list of specified, noncompetitive imports, the terms of reciprocity were definitely prescribed by law and might be put into effect by the President without further action by Congress. A number of reciprocity agreements were entered into with foreign governments under provisions of this nature. However, the scope of trade covered thereby was very narrow and the benefits resulting therefrom correspondingly limited.

In respect of other imports, including those of a competitive nature, the provisions for reciprocity contained in the act of 1897 did not prescribe specifically, except for certain limits, the treatment to be accorded, but did require that action taken by the President thereunder be subject to Congressional approval and Senate ratification. Although a number of reciprocity agreements were concluded under these provisions,

none obtained Senate ratification, and none, therefore, ever came into effect.

The failure of this reciprocity to achieve notable success under a régime of aggressive protectionism may be readily understood if we contrast the principle of reciprocity with the cost-of-production principle which was later explicitly adopted as the basis of Republican high tariff policy. Reciprocity is a trade-promoting principle; it secures increased opportunities for export trade by providing reciprocal opportunities for import trade. Under the cost-of-production principle, the stated function of import duties is to equalize the differences between production costs at home and abroad, and thereby to offset advantages of foreign producers over domestic producers in selling in the domestic market.

Differences in costs and prices constitute, of course, the fundamental basis of trade. The fact that American costs of producing many agricultural, mining and manufactured products are lower than foreign costs accounts for the existence of our export trade. A principle which envisages the international equalization of production costs may lead to the most extreme type of protectionism, and, if followed with logical thoroughness in application to all commodities, it would result in a virtual breakdown of our foreign trade. In actual practice, however, it has not been followed with such consistent thoroughness.

In application the principle may be qualified by restricting it to duties on so-called competitive products. This apparently clear-cut distinction becomes more ideological than real, however, when the task of classifying the actual commodities of trade into competitive and noncompetitive is essayed. There are some products, including especially certain raw materials, with respect to which the imposition or increase of duties would be strenuously opposed by the industries requiring them, even though in some cases such industries may enjoy tariff protection for their finished products. There are, as a matter of fact, relatively few articles which could not be produced in this country, or at least domestic substitutes found for them, if the import duties are sufficiently high.

Our import duties are high enough in some instances to permit the growth of certain hot-house fruits and vegetables for sale in the home market during the " off season ", and im-

ports during that season of naturally grown products from warmer countries are, of course, regarded as competitive with those of the American hot-house industry. Import duties on bananas have been advocated, not to encourage banana growing in the United States, but to discourage the eating of bananas by Americans in order that they might eat more apples.

The truth is that the significance of the distinction between "competitive" and "noncompetitive" products depends, in application, upon the degree and directness or indirectness of competition which is taken as criterion, and this is not easily defined as a general principle. In fact, it is in some cases perhaps not too far from the truth to conclude that the real distinction, as applied under high-tariff policies, is little more than a segregation of products for which there is no strong interest demanding protection, or for which the opposition to protection or increased protection is strong enough to prevent it.

The limits to which tariff protection can be carried under a so-called equalizing of cost-of-production policy, even distinguishing competitive and noncompetitive products, are vague and indefinite, and appear to be determined, not by considerations of what is good for the nation as a whole, but by the energy and political influence of individual interests. In circumstances in which an effort is made to pursue a program of reciprocity in conjunction with an aggressive tariff policy, to which the principle of cost equalization gives rise, reciprocity is relegated to a restricted and relatively unimportant field of operation. It may be pursued only in respect of so-called noncompetitive imports. In other words, it is limited to a field in respect of which there is no effective demand for the existence of tariff protection, or in respect of which the extension of such protection is strongly opposed by domestic interests. Foreign countries are not likely to provide substantially increased export opportunities for our products in return for a promise from us not to raise barriers which it would be to no one's interest to raise.

On the other hand, the principle of reciprocal tariff adjustment provides a much broader and sounder basis for protection of American production and trade than that which rests on the basis of excessive tariffs framed only from the point of view

of the individual domestic interests demanding protection. In addition to providing for the protection and expansion of foreign markets for American products, it envisages also *reasonable* protection of the home market for home producers. In the determination of what is reasonable in this respect, it is possible to take into account under reciprocity, not only the problems of the high-cost industries, but also those of other industries, together with the general interests of the nation as a whole. All of these aspects are taken into full account in the adjustments of import duties effected under the present reciprocity program of the government.

Another element of the trade agreements program is the reciprocal and unconditional most favored nation principle, under which we extend to, and receive from, other countries automatically and unconditionally customs treatment which is no less favorable than that accorded to the most favored nation. In other words, it provides that each country shall grant the other treatment as favorable as that granted to any third country with respect to each of its products.

The most favored nation principle is necessary in order that the benefits obtained under reciprocity may be safeguarded and preserved. Suppose, for example, we obtain in an agreement a reduction in a foreign country's duty on, say, lard from 50 per cent ad valorem to 25 per cent ad valorem. If, after our agreement is concluded, the foreign country should make an agreement with a third country and reduce the rate to 10 per cent, while we continued to pay our contractual rate of 25 per cent, the value of the concession would be destroyed because our competitors would take the market. Most favored nation assurances prevent this by requiring that the rate of 10 per cent be immediately extended to us. Thus, the most favored nation clause prevents the concessions we obtain from being undermined by the extension of greater concessions to our competitors which are withheld from us.

Not only is provision made in trade agreements for reciprocal most favored nation treatment in respect of trade between the United States and the other countries with which agreements are concluded, but also the Trade Agreements Act requires that the concessions granted to these countries under reciprocity agreements be extended to third countries which do not discriminate against our trade; any other course would

impel nonagreement countries to resort to retaliatory discriminations against us and thus contribute to the process of discrimination and retaliation which have been responsible in a large measure for the international commercial breakdown of recent years.

The provision for unconditional most favored nation treatment under the trade agreements program does not represent a departure from the established practice in our international commercial relations. The principle was formally adopted in 1923 during the Harding Administration. This principle is, moreover, one phase of the basic concept upon which our trading policies are founded. George Washington, in his Farewell Address, advocated equality of treatment toward all nations. He said:

> Harmony, liberal intercourse with all nations are recommended by policy, humanity, and interest. But even our commercial policy should hold an equal and impartial hand, neither seeking nor granting exclusive favors or preferences; consulting the natural course of things; diffusing and diversifying by gentle means the streams of commerce, but forcing nothing.

In order to use our tariff bargaining power to the greatest advantage under the most favored nation principle, it has been our general practice to grant to another country in a trade agreement concessions on those products of which that country is the chief or an important supplier in our import trade. A concession on an imported product ordinarily means more to the major supplier of that product than to any other supplier and, therefore, usually represents the most effective use of our bargaining power with respect to the commodity in question. Not even the chief-supplier rule is altogether new. A precedent for it may be found in the Republican tariff acts of 1922 and 1930. The "flexible provisions" of those acts require that the differences in costs at home and abroad shall be determined with reference to the production costs of the chief competing country or chief supplier.

A system of reciprocity might be conducted on the basis of a detailed specification by Congress of the precise treatment to be conceded in reciprocity agreements. This was done, as I have stated, in certain reciprocity provisions of the tariff acts of 1890 and 1897. Such procedure, however, seriously

limits the degree and flexibility of action and therefore the extent of the benefits to be secured for our exports, since it restricts the extent of adjustment to the other country's needs and desires which may be effected by negotiations.

The more satisfactory procedure is that of tariff bargaining, whereby, within the limits authorized by law, the concessions to be granted the other country are fixed in the process of negotiation, in accordance with that country's needs and desires and in consideration for the reciprocal concessions obtained from that country. This makes possible the most flexible and effective use of our bargaining power, maintaining on the one hand due regard for the position of domestic protected interests by avoiding any concessions involving tariff reductions more extensive than the circumstances justify, but permitting the actual concessions to be formulated in the light of what the other country is most willing to pay for.

Tariff bargaining is, of course, not new in our tariff policy. It was provided for in the reciprocity provisions of the tariff act of 1897, pertaining to imported products not specified, including competitive imports. Since the results of bargaining under those provisions were subject to Congressional approval, and since such approval was not obtained in the case of a single agreement, the benefits to be derived by this method were never realized.

Under our system of political institutions and procedure, a limited but adequate measure of Congressional delegation to the Executive of authority to make tariff adjustments is a practical essential to a successful working policy of tariff reciprocity. The alternative, the requirement of subsequent Congressional approval of agreements reached, has been shown by experience not to be practicable and effective.

The delegation of authority to adjust tariff rates within prescribed limits and by prescribed procedure does, however, involve important considerations which have lately been receiving much attention. Under the Constitution, the President conducts negotiations with foreign governments, whereas the formulation of tariff policy is a legislative matter. The bridging of this division of powers between the legislative and executive branches of the government is effected in the Trade Agreements Act by Congress delegating to the President authority to adjust rates of import duty, within prescribed

limits and in accordance with prescribed principles, and invoking the power of the President to enter into international agreements in connection with the exercise of this delegated authority. The question of constitutionality which has been raised with reference to the Trade Agreements Act involves the Congressional delegation of authority to adjust tariff rates.

Congressional delegation of authority to fix tariff rates is not new. It is provided for in the flexible tariff provisions of the Republican tariff acts of 1922 and 1930, and has been upheld by the Supreme Court of the United States. With reference to this question in the case of *Hampton Co.* v. *U. S.*, Mr. Chief Justice Taft said:

> If Congress shall lay down by legislative act an intelligible principle to which the person or body authorized to fix such rates is directed to conform, such legislative action is not a forbidden delegation of legislative power.

In its report of March 8, 1940, recommending the passage of the joint resolution to extend the Trade Agreements Act for another three-year period, the Committee on Finance of the Senate stated:

> The limitations and policies prescribed in the Trade Agreements Act constitute an "intelligible principle" or standard for the guidance of the Executive which is in no degree less precise than the standards contained in the "flexible provisions" of the Tariff Acts of 1922 and 1930, and the prior reciprocity statutory authorizations, all of which have been sustained by the courts.

The procedure provided for in the Trade Agreements Act for effecting tariff adjustments is in accordance with long-established practices of democratic government. As in the case of the fixing of tariff rates by legislation or by executive proclamation under the "flexible tariff provisions" of the law, an opportunity is given to all interested persons to present their views before any action is taken.

Moreover, in view of the growing complexity of our economy and the highly intricate and technical problems involved in tariff changes, the provision under the trade agreements procedure for expert study and analysis in the formulation of detailed recommendations is of high importance. Such expert study and assistance have, of course, been available in the present Tariff Commission since its establishment in 1917

under a Democratic administration. Somewhat similar organizations had been established before that time under Republican administrations. In 1882 Congress passed an act for the appointment of a tariff commission. A tariff board was also provided for in 1909.

The Trade Agreements Act provides, however, that before any agreement is concluded, information and advice shall be sought not only from the Tariff Commission but also from the Departments of State, Agriculture and Commerce, and from other appropriate sources. The technical problems of the tariff lying within the purview of the Tariff Commission constitute only one group of problems involved in tariff adjustments under the principle of reciprocity. There are also many other types of problems requiring consideration, such as those involving export trade, foreign commercial policies, international relations and relationships between various industries and branches of our economy. An interdepartmental trade agreements organization, composed of representatives of the various departments and agencies of the government concerned with such problems, was established to carry out the work of the trade agreements program. Machinery has been established for making readily available to this organization information, advice and technical assistance from government sources and information and views from private interests, in order that all may be brought to bear in a coördinated and expert fashion on the problems arising for consideration. The need and provision for such guidance testify to the broad basis of national interest on which this program rests.

The trade agreements program seeks, of course, to reduce excessive rates of duty on imports into this country. This is not the first time, however, that such a purpose has been pursued in our tariff history. It has been followed under previous Democratic administrations which have traditionally been opposed to excessive tariff protection.

A great development has occurred in our national economic complexion since the founding of this Republic, and tariff making has become a very intricate and complex matter since the enactment of the first tariff act of July 4, 1789, which contained only some thirty classifications. Congress has found rate fixing an increasingly difficult task and has introduced into tariff making over a period of years a number of elements

to improve and facilitate the work. The writing of tariff schedules has, however, become far too unwieldy and technical for Congress to undertake.

Concern for the preservation of democratic processes under the complexities of modern industrialism has compelled increasing recognition by legislatures of the necessity of concentrating their attention more and more upon the problem of determining general policy and the establishment of broad rules of guidance for its execution. The details of administration are necessarily left to the executive branches of government. The effective operation of the trade agreements program has been established on a practical evolution of this principle.

I have pointed out that none of the essential elements involved in the principles, methods and procedures of tariff making under the trade agreements program is new. Reciprocity itself is an old principle. The selection of other elements which in combination with it form the trade agreements program was made with a view to giving the fullest effect possible to the principle of reciprocity. However, the combination of these various elements represents a new development in our tariff history. Congress has provided in the law, principles and procedures for adjusting tariff rates within specified limits, but the technical work of fixing specific rates in accordance with these directions is turned over to the executive branch of the government. Since the Executive, in the exercise of his authority, is required to follow the provisions of the law, logrolling and sectional pressure are no longer determining factors in rate fixing.

By the so-called flexible tariff provisions of 1922 and 1930, based upon the Republican cost-of-production principle, it was hoped to attain such an objective, but, owing in large measure to the defective nature of this principle, the effective scope of these provisions has in practice been extremely limited. According to Thomas Walker Page, former Chairman of the Tariff Commission, "The conclusion cannot be escaped that it is rarely possible to ascertain accurately the differences in cost of production at home and abroad." Experience has shown that the cost-of-production findings cannot be completed short of months, sometimes a year. During the eight years in which the act of 1922 was in force, out of several thousands of items

in the tariff schedules, only thirty-six tariff adjustments were made and only sixty-two have been made under the "flexible provisions" of the act of 1930. Under the trade agreements program, however, the means which has been found for freeing tariff making from the influence of tariff lobbies has actually been applied in a broad field of operation.

While this achievement represents a marked advance in tariff making, its great significance lies in the circumstances out of which this change grew. This country has at last come to recognize that tariff making is not solely a matter of domestic policy but involves our relations with the rest of the world. We came to realize from the shock of the depression of 1930-1932 that the world is economically interdependent, that our prosperity is dependent on the prosperity of other countries and on reasonable opportunities for mutually profitable international trade, and, finally, that peace, as well as prosperity, can exist only on a sound basis of international coöperation. Appreciation of the fact that tariff making affects our national livelihood and political security has raised it to a place of utmost importance in the minds of serious-thinking Americans, and accounts for the establishment of the trade agreements program. In view of its new use under that program as an instrument for coördinating our national and foreign policies for the attainment of prosperity and world peace, tariff making must not again be permitted to serve as a plaything of politics.

Remarks by the Chairman

President Mitchell: Our next speaker will be Mr. Edward A. O'Neal, President of the American Farm Bureau Federation. His topic is "The Farmer under the Trade Agreements". Mr. O'Neal!

THE FARMER UNDER THE RECIPROCAL TRADE AGREEMENTS

EDWARD A. O'NEAL
President, American Farm Bureau Federation

THOUGH I am not a stranger in a strange land, perhaps I had better take a moment to tell you whom I represent. I represent a national farm organization which has thirty-nine state units and one thousand seven hundred forty-one counties of organized farmers in the United States, all the way from Maine to California.

The farmer probably has more at stake in foreign trade than most other groups, not only because America's agricultural plant, like our industrial plant, is capable of producing far beyond the needs of the domestic market, but also, and primarily, because it is more difficult for the farmer to curtail his production than it is for a manufacturer to do so.

There is no need to dwell unduly on the overexpansion of plant and equipment, both industrial and agricultural, which took place during the first World War, because all of you here are intimately familiar with the facts. We cannot disregard it, however, in considering the problem of surpluses which has plagued the farm economy of this country almost continuously since 1920. Farmers plowed up 40,000,000 additional acres of land to meet the war demand for food and fiber. Expanding the productive plant by that much is bound to be a huge and hazardous undertaking for farmers, due to the nature of the farming business. There is no quick turnover in agriculture as there is in manufacturing. The production cycle is slow and measured, subject to tremendous hazards of wind and weather, pest and parasite. The shortest cycle is one year, for most crops, and two years and more in animal production. A good crop rotation extends over three or four years. If the average productive lifetime of farmers is thirty years, then during a farmer's career there is time for the completion of only ten rotations. Farming is not a business that you can get in or out of quickly, and, once in, it is

a difficult matter to alter a rotation or change a type of farming within a short time.

At the close of the War, our foreign markets collapsed. Our former customers had become our debtors, instead of creditors as they had been in pre-war days. They had no money to pay for our commodities, and our tariffs effectively prevented them from exchanging manufactured goods for our commodities in any great volume.

These factors combined resulted in surpluses so large as to keep farm prices almost continuously out of line with industrial prices and industrial wages. The farmer steadily improved his productive efficiency (farm output per worker is now 21 per cent higher than in 1910-1914, and output per acre is 12 per cent higher), but these gains were not enough to offset the price disparity which prevailed. The American farmer is now the most efficient producer of food and fiber in the world. As *Fortune Magazine* said in its February issue, " the gargantuan production of foodstuffs in the United States is unparalleled on earth. . . ."

Fortune said further:

> The achievement of the farmer is precisely the achievement of the industrialist: he has succeeded in producing more with less. Whereas in 1787, when the Constitution was framed, the surplus food produced by 19 farm people went to feed one city person, today 19 people on farms produce enough food for 56 non-farm people in the United States plus 10 living abroad. Nothing like this has ever been achieved before. It is an achievement that enabled the United States to obtain and service the huge drafts of foreign capital necessary for the rapid building of railroads and industries during the second half of the nineteenth century. Indeed it is clear that the farmer historically has subsidized the manufacturer and the railroad builder, quite aside from any additional subsidy in the tariff. But the farmer's achievement, since it formed a part of the industrial system, has generated the typical industrial problem. The farmer has too much of everything; too much capacity, too much product, too much labor. Like the industrialist, he appears to have done his job too well . . . .

Industry, its prices protected by tariffs, could get along by holding production to a volume that could be absorbed by the domestic market at a price profitable to the manufacturer. But agriculture, competing with the world and unable to adjust production without help from the government, continued to produce beyond the needs of the market, and world prices became the American price for most farm products.

The farmer's attitude on the tariff and administered prices is nicely summed up by William Hard in the January issue of *The Reader's Digest:*

> The farmer labors under an extreme domination. He is a manufacturer of agricultural goods. If you want to know the price of a Plymouth, you essentially ask Mr. Chrysler and take it or leave it. But if you want to know the price of grain, do you ask the farmer? You do not. You ask the market report—over which, generally speaking, the farmer has no control whatsoever.
>
> Suppose that Mr. Chrysler shipped out his Plymouths and then had to read the newspapers or listen to the radio to find out what price Plymouths were getting in a Chicago automobile board of trade. Would he go red-eyed?
>
> The farmer has been red-eyed for just that sort of reason for 50 years. No man is a free man when his prices are utterly dictated by others. The farmer is out to get his own sort of collective bargaining. To do it he will invoke government.

The American Farm Bureau Federation was organized at the close of the first World War, and for twenty years it has devoted its energies to the problem of the farm surplus. The historic fight for the McNary-Haugen Bill was based on the demand by farmers for some method of segregating the surplus so that it would permit the law of supply and demand to operate on a domestic basis. Industry had already succeeded in this, and farmers saw clearly that unless they could accomplish the same thing in a different way, they could not reach parity with industry. The McNary-Haugen plan would not work today, due to the strong nationalistic policies of foreign nations, but if it had been adopted at the time, it probably would have made the tariff effective for agriculture.

Those who maintain that the foreign market for agricultural products is insignificant simply do not understand and fully appreciate the facts. During the period of 1928 to 1937, nine years, when the situation was not particularly favorable to foreign trade, the export market took 52 per cent of our cotton, 40 per cent of our dried fruits, 35 per cent of our tobacco, 21 per cent of our lard, 16 per cent of our rice, 15 per cent of our canned fruit, 11 per cent of our wheat and flour, and 8 per cent of our apples. Those volumes are sufficient in every case to make a tremendous difference in the domestic price. But we did not export enough to raise domestic prices to satisfactory levels; and so we had to have acreage adjustment programs.

The protective tariff, together with monopoly privileges and other artificial devices employed by industry and labor, is, of course, at the bottom of the disparity in prices between agriculture and the other segments of our national economy. In recent years Congress has enacted laws designed to give farmers some advantage to offset the disadvantage which resulted from the protective tariff. In other words, a tariff-equivalent for agriculture.

Under these programs, farmers out of their abundance pool reserve supplies in the national ever-normal granary to guard against possible scarcity, and then to adjust production to meet current demands. In effect, the farmer guarantees the consumer abundant supplies at fair prices, even though he knows that large supplies have a bearish effect on price. In partial offset are the commodity loans which place a floor under market prices, as low in some instances as 52 per cent of parity. The consumer is protected in far greater degree than is the producer.

To the man in the street this system will doubtless seem clumsy and unwieldy in comparison with the automatically operating tariff system and corporate controls that protect our industrial prices. The farmer knows that his program suffers in this comparison, but it is the best that he has seen, and so he goes along with it. As a farm leader I have often dreamed about and yearned for some protective device for agriculture which will function with the ease and certainty of the protective tariff. But so far no such device has appeared.

In January of this year prices received by farmers averaged 99 per cent of pre-war, while prices paid by farmers for supplies and equipment averaged 122 per cent of pre-war. In other words, the farmer is at a disadvantage of practically 20 per cent with other groups, and as long as that condition continues, he cannot buy the products of industry and labor in normal volume. The industrial tariff has imposed heavy penalties on the farmer. According to a recent estimate by the United States Department of Agriculture, assuming that the tariff is fully effective, the tariff in 1935 cost no less than $108 per farm family. Even though not fully effective, the actual cost to farmers is large, and it amounts to a substantial item in the farmer's annual budget.

At the time of my appearance before the Ways and Means Committee of the House, I was astonished to find that one of the authors of the Smoot-Hawley Tariff Bill did not know what was in it. He denied that the tariff is effective. I challenged him to show me an article on his person, starting with the soles of his feet — and he did not have any false hair, either—that was not protected. He was not able to do so.

Because of its adverse effect on the farm economy, I do not take the position that the tariff is wholly bad. I do believe that we in this country have carried the tariff principle far beyond the point of diminishing returns; that it has, in effect, brought about an "economy of scarcity" in this country. I believe that it must be modified sufficiently to enable us to recover a share, at least, of the rich foreign commerce that we once had. I know of no better method of doing this than through the reciprocal trade agreements program, which supplements the A.A.A. programs very effectively.

The crying need of the nation today is for greater production and use of goods and services, and that can come only with reduced prices for manufactured goods. Reduced prices can be achieved through the greater volume of production that will be needed with enlarged foreign outlets. The American farmer challenges industry and labor to coöperate with him on a national program of increased production at lower prices.

The farmer's goal of parity is simply a price which will enable him to buy as much, in goods and services, as he could buy with the same commodities in the 1909-1914 period. If industrial prices can be brought down through increased production, then the parity figure is reduced correspondingly.

We all know that the dividing line between profit and loss in a mass-production industry is very narrow. The automobile industry is a good example. After a certain point in volume of production has been reached, profits rise in geometric ratio. Additional production of only 10 per cent may mean 100 per cent increase in profit to the manufacturer. In my opinion, that extra 10 per cent or 15 per cent that might be sold abroad is the key to further progress for our industrial economy as well as our farm economy.

So much for the objective. The question is how to attain it. During the exhaustive hearings conducted by Congressional

committees on the continuation of our reciprocal trade agreements policy, there were very few witnesses who advocated a return to the practice of tariff revision by Congress. Too often in the past, revisions have been the result of individual trades between lawmakers—logrolling of the worst sort. In practice, this system is simply impossible.

Reciprocal trade agreements, it seems to me, have proved to be a practicable and effective means of modifying tariff policies, in spite of disturbed world conditions. All of you are familiar with the extreme nationalistic policies which have dominated nations which formerly were our good customers. You are also familiar with the retaliatory action of many nations in protest against our Hawley-Smoot Act of 1930. You cannot reverse such a trend overnight, or within a few years, particularly in years when nations were straining their resources in preparation for war. If only we could have had a Reciprocal Trade Agreements Act immediately following the first World War, when in all nations there was a crying need for more goods and commodities, and plenty of labor available to produce goods for trading purposes, I believe the results would have been far more striking than they have been since 1934.

Results of our trade agreements to date have not been spectacular, but they have been in the right direction. A study by Dr. T. W. Schultz and his associates at Iowa State College last year, covering trade agreements involving 88 per cent of our trade under such treaties, revealed that exports to trade agreement countries in 1937 and 1938 had increased 61.2 per cent over 1934 and 1935, while exports to non-trade agreement countries had increased only 37.9 per cent. The very substantial increase in exports to trade agreement countries certainly must be considered quite significant, particularly when volume of imports from trade agreement countries during the same period increased at practically the same rate as from non-agreement countries.

Careful study of the entire situation impelled Dr. Schultz and his associates to report:

> We cannot expect to find spectacular results from the trade agreement program because the State Department, as a matter of choice or necessity, has not been spectacular in its methods. Talk by politicians

and propagandists to the contrary notwithstanding, nobody has been "sold down the river" by the trade agreements. More drastic general action would have hurt some groups or producers. It undoubtedly would have helped others . . . .

In spite of the difficulty of cutting through such obstacles to appraisal, the material presented in the earlier reports all tends to the same general conclusion. The trade agreements have been doing their job . . . .

It has been charged that many American wage-earners have lost their jobs as a result of influxes of manufactured goods into this country because of reciprocal trade agreements. Dr. Isador Lubin, Commissioner of Labor Statistics, Department of Labor, has answered this charge by pointing out that average annual exports of manufactured goods to trade agreement countries in the years 1937 and 1938 were $353,000,000 more than in 1934 and 1935; while dutiable imports from those same countries had increased only $88,000,000.

The fact is that agriculture, industry and labor all have a big stake in increased foreign trade. All groups in this country are interdependent, and if one gets more than its share, then one of the other groups must necessarily accept less than its fair share. The only way in which all can benefit is through maintaining fair economic balance among the groups, and then to go ahead on a national program of increased production and use of goods.

But I do not believe that we can consume all that we can produce. I believe we simply must export a good share of our production. We are just too efficient in our technology, both in agriculture and in industry. Our tremendous increase in efficiency, added to the change in status of this country from debtor to creditor following the first World War, obviously called for a new approach to the problem of foreign trade. But instead of trying to find a new approach, we continued with the old protectionist philosophy and carried it, in 1930, to an extreme never before approached. This policy hurt the farmers worse than any other group, because agriculture depended on the export market to absorb its surpluses.

To give you an idea of the tremendous importance of our export market, let me remind you that in 1923 we exported the colossal volume of nearly 2,000,000,000 pounds of pork products, or the equivalent of some 18,000,000 hogs, or practically one third of all hogs marketed that year. After the

adoption of the Hawley-Smoot Act in 1930, our exports declined steadily. In recent years we have exported less than 10 per cent of the 1923 volume. The loss of that market has been one of the hardest blows that American agriculture has suffered.

Foreign markets historically absorbed from 50 to 60 per cent of our cotton, more than a third of our tobacco, 24 per cent of our wheat and wheat products, along with tremendous quantities of other commodities. Because foreign outlets absorbed our surpluses, prices in the domestic market were consistently at parity levels during the pre-war period of 1909 to 1914.

Now I want to say a few words about a phrase that many of you have heard and that has a very wide appeal to farmers. It is "The American Market for the American Farmer". It is used by opponents to the reciprocal trade program, the implication being that somehow the program is giving part of the American market to the producers in some other countries. The phrase sounds well, but let us examine the facts. Maybe we have now the equivalent of more than the American market for the American farmer. Maybe we must have more than the American market to attain prosperity. In recent years we have had for ourselves 93 to 94 per cent of the domestic market, nearly 3 per cent more than we had in 1928 and 1939.

If we were to adopt that slogan, and keep all of our own market for our own producers, to be consistent we would be compelled to grant to every other nation the same prerogative—in other words, all nations would be 100 per cent nationalistic with respect to competitive products. What would happen to our cotton producers under such a set-up?

During the fiscal year 1937-1938, the last year for which we have complete official records, the farm products we imported could have been produced on 7,564,000 acres of our land. But our farm exports in that year required 36,367,000 acres of land, or nearly five times as much as were required to grow the products we imported. In other words, American farmers actually enjoy much more than the American market now; and if we were to cut off both our exports and imports of competitive products, we would have to shrink our productive plant by at least 28,000,000 acres, or more land than we

now devote to cotton growing, one of the great staple products in this country. And remember that 13,000,000 people depend upon cotton for a large part of their cash income. To me that completely annihilates the argument of those who want to restrict the American farmer to the domestic market.

Extravagant claims are often made by those who profess to believe that we should reserve the home market exclusively for our own farmers. For example, it has been stated repeatedly that if we would bar all sugar imports and grow sugar beets enough to supply the domestic market, our beet acreage could be increased by 24,000,000 acres. That is more sugar than is grown anywhere in the world. Examination of the facts reveals that we import only 3,910,000 short tons of sugar. We could easily produce that tonnage on 2,400,000 acres of beets, or about 10 per cent of the acreage claimed by the sponsors of the embargo idea. I mention this to show how important it is to get the facts before we make up our minds on questions of such great importance.

During all the history of the world, the prosperous nations have been the trading nations. An active world commerce is stimulating to all trade. The most prosperous years that our own nation has experienced have been years when imports, as well as exports, have been greatest. Most of the wars of history have been caused by trade or other restrictions imposed by the stronger nations upon the weaker ones. I do not hold to the belief that this nation should be the custodian of peace throughout the world, but I do know that at the end of the present world conflict our country will be in a position to have a tremendous influence on the course of world events. I earnestly hope that that influence may be on the side of more liberal trade relations between nations and that our example may be a wholesome one for the unfortunate nations which have foundered on the rocks of narrow internationalism. For our own sake, as well as for the sake of the nations that will be reduced to comparative poverty for a long time to come, I hope that we may take the lead in adopting policies which are based on a broad, constructive philosophy. The objectives of such a philosophy may be realized and attained among the nations, just as they may be attained among groups within a single country.

Remarks by the Chairman

President Mitchell: Our next speaker is Mr. Emil Rieve, President of the Textile Workers Union of America. He has for his subject " Trade Agreements and Labor ". I have the pleasure of introducing Mr. Rieve!

TRADE AGREEMENTS AND LABOR

EMIL RIEVE
President, Textile Workers Union of America

THE extension of the Trade Agreements Act by Congress removes the question of its advisability from the realm of pressing concern and projects the problems and principles of its administration to the forefront. Our State Department will negotiate reciprocal tariff agreements with foreign countries. They will provide specific concessions to them and ourselves. We are interested in presenting labor's interests in these deliberations. What does the American worker expect?

Representing textile workers, I shall present their attitude on the basis of the proposals which have already been offered in trade treaties negotiated by the State Department. The textile industry is international in character, perhaps more so than most industries. Most countries have substantial textile industries of their own. Many areas, which until recently had been colonial in character and had served as markets for mature industrial nations, have built textile industries of their own which not only supply their needs but also export to other countries. These nations, moreover, have equipped themselves with most modern machines, procedures and practices and thereby gained a competitive advantage over older countries with older and sometimes obsolete equipment. Free commerce in textile machinery has brought technological developments to all buyers in all parts of the world. The relatively small size of the basic manufacturing units and the ease of operation as well as the abundance of labor have made it feasible to employ the equipment in these countries. New and cheaper fibers are being used. Moreover, textile fiber prices are for the most part set in world markets and are uniform for all. As a result, the major differences in competitive cost among textile countries rest with the labor factor. Nations paying lower wages, working their textile workers longer hours, and imposing larger work assignments are the ones which manu-

facture the products at the least cost. Competition is world wide. The dependence of many countries upon the success or failure of their textile industry makes them ever eager to penetrate available markets. The American market is particularly attractive to them to balance purchases made here or to accumulate dollar balances for purchases in other sections of the world.

This desire of foreign countries to secure a foothold in our textile market has been a real threat to the textile worker. Earnings in foreign countries have been relatively lower than those in this country, and working hours have been longer. Before the present war English and German textile workers were receiving one half to one third of the American standard, and Japanese workers were receiving only one twentieth of the present American rate. While the standard working week in the United States was 40 hours, only a few European countries boasted of a similar work week and these have extended their working hours with the announcement of the present war. Working hours of Asiatic workers ranged from 9 to 11 per day, while most European countries observed a 48-hour week. Competition with these labor conditions is impossible. American textile workers do not believe that it is in the best interest of this country to sacrifice its labor standards for a larger trickle of foreign trade.

It must, moreover, be underscored that even though the earnings of the American textile worker are the highest in the world, they are among the lowest received by American industrial workers. Whereas the average hourly earnings in manufacturing industries in this country is 64.5 cents per hour, the average hourly earnings of the American cotton textile worker in the South is 39.2 cents and 46.9 cents in the North. These earnings have been secured after a long uphill fight by unions and support by federal legislation. The textile worker is anxious to increase his earnings at least to the level of other American workers. He is very desirous of having his present standard protected and of preventing any disturbing factors from being introduced into the industry which will increase the difficulties of securing higher standards.

The existence of these high standards should be an additional reason why America should lead in advocating further improvements in working conditions in all countries. The Amer-

ican textile industry and the government have in fact assumed the leadership in an international effort to establish a standard forty-hour week. It invited the International Labor Office to hold its textile conference in this country and supported the adoption of the international convention. We can do more to establish international good will by supporting and ratifying this convention and continuing our leadership in this field than by arranging a slight increase in international trade. By constantly improving labor standards throughout the world we are developing the best guarantee for world peace.

In negotiating new agreements, special consideration must be given to the increasingly common practice of dumping goods in this country at almost any sacrifice in order to gain their entry. The dumping of goods at artificially lower prices intensifies the existing advantages in lower labor cost which these countries now possess. Particular protection must be assured the American textile worker against such dumping.

The importation of textile products into this country in competition with American products can have a most harmful effect on the interests of textile workers. Already textile workers face many disturbing threats which have made their position most insecure. The industry is highly competitive and is one in which there are periods of overproduction followed by liquidation and unemployment. Work is seasonal and irregular. These disturbances are aggravated by intra-industry competition which, for example, doomed the silk industry, increased the use of spun rayon, and granted special importance to the worsted industry at the expense of the woolen industry. Even though most branches have been maturely developed for over fifty years, mechanical progress has continued at such a rate that though textile fiber consumption during the last twenty years increased over 25 per cent, during the same period total man hours declined 20 per cent. Employment is now about 10 per cent lower than in 1923, despite the reduction of the work week from 55 to 40 hours.

The instability of the industry has been intensified by migration. Entire textile communities are depressed as textile mills have moved out of them. Threats of further migration are still serious. Any tariff changes which will introduce an additional factor of instability will tend to reinforce these diffi-

culties and problems of the textile industry which as yet neither the industry nor government has satisfactorily handled.

Foreign trade policies which will throw additional numbers of textile workers out of employment will increase their problems in an industry which is declining in importance as a source of employment and minimize possibilities for progressive improvement and stabilization.

There is little need for removing tariff protection for textile products to assure lower costs. The industry has made phenomenal advances in technology and in the reduction of costs of operation. Man-hour productivity in cotton textiles has risen 77 per cent between 1919 and 1939; in the woolen and worsted industry, 80 per cent; and in the synthetic yarn industry, 333 per cent from 1923 to 1939. Competition is widespread and effective in this industry. Wholesale prices have dropped 58 per cent from 1919 to 1939. New types of yarns, new fabrics, new products are constantly being manufactured. The removal of present tariff protection will not promote additional technological change nor affect monopoly profits, as technical innovations are being introduced as rapidly as they are proved practical, and monopoly profits fostered by tariff protection are practically nonexistent.

The elimination of profitable outlets for part of the existing equipment will increase over-capacity and make competition keener for the shrinking market. The American textile industries will make a greater contribution toward our national well-being by improving the earnings of its employees than would be possible through any savings in price due to the importation of low-priced textiles from foreign countries, or through the possible slight increases in imports which may follow from concessions to foreign countries. The price for increases in textile imports is too great to be paid without protest from textile workers.

The advocates of reciprocity treaties have recognized the soundness of the above position and have recurrently undertaken to assure labor that wage and working standards would not be sacrificed or that the increased volume of trade following from a more active export industry would compensate for the immediate loss in the domestic industry by increasing national income, thus ultimately expanding the demand for domestic products. Such was Mr. Hull's position in his letters

of May 15, 1939 and January 16, 1940, to the President of the Continental Mills of Philadelphia, Pennsylvania. We cannot place much reliance on possible ultimate resolution of the problem, while immediate concessions will now certainly throw thousands of textile workers out of employment and create greater dislocations in the industry.

The export industries have suffered greatly from the appearance of nationalistic economies throughout the world. Centralized control of foreign trade, high tariff barriers, exchange restrictions, quota regulations, export subsidies, import prohibitions and preferential treatments have changed the course of foreign trade. Nationalistic economies aiming to make their countries self-sufficient have changed the nature of the trade of foreign countries. Foreign trade does offer many advantages but now can be bought only at a very high price to domestic industry, and at a great hazard, since abrupt changes in need or the direction of trade are highly possible and probable in our present international scene. The whims of foreign dictators or extremely nationalistic economies may at a moment's notice completely destroy foreign markets and thereby eliminate the outlets for industries depending on such markets. It is particularly dangerous to expand international trade with methods which involve any sacrifice of American interests since the advantages may disappear through sudden alterations in the policies of foreign countries. It is, therefore, important to reorient American foreign trade policies and to make them more realistic and more deeply aware of the present nature of international trade. We must depend more fully on trade only in materials in which we possess some advantage or which we really need to acquire.

America is interested in the continuance and expansion of foreign trade. Its industries which depend upon such trade can benefit directly by securing new markets. American industries which consume foreign products secure their raw materials from other countries. Foreign trade either provides the consumer with goods which he could not obtain in this country or offers them at very attractive prices. Foreign trade cannot be stimulated by any of the current proposals related directly to such foreign demand. There is much consideration of foreign loans. But this is a very delusive method of expanding foreign trade. It creates more problems than it solves.

During the twenties, billions of dollars of American goods were sent to Europe by reason of large loans granted by American financiers. The results are well known to all of us. They aggravated our unstable economy and stimulated speculative expansion of many industries. These loans in part created the basis of the depression of 1929-1933. They fostered the development of export goods industries, particularly capital goods which could not find a market in this country. When our financiers were no longer willing to continue this export of American goods, the industries collapsed. Foreign loans also created trouble for the future when payments have to be made. This country is finding it difficult to shift to the so-called creditor position. Dislocation and unemployment became widespread. The conflict of interests between the investors in foreign loans and the investors in American export industries became a source of real national tension.

No such artificial stimulant to foreign trade can be approved by labor. The primary method for expanding this trade must be found in our own national economy; an expanding national income and an increased demand for domestic and foreign goods. The more we consume, the more foreign raw materials we need and the better prepared we are to accept foreign goods. Increased importation, predicated on the basis of a greater demand for foreign goods, is the normal and soundest basis for international trade. It sacrifices no national group; it focuses interest on internal problems; and it assures the greatest market for foreign goods. It establishes the safest basis for general well-being.

In developing foreign trade policies, as in the midst of highly controlled centralized national economies, our government must think only in terms of our national best interests. In so far as international trade is concerned, the price mechanism is no longer fully operative. An increasing number of foreign countries are controlling their purchases and allocating their foreign balances in terms of their own defined interests. Foreign trade is being planned. While we cannot approve of their purposes and methods, we must be realistic enough to recognize their existence. In view of these changes, we must control our foreign trade in a more conscious manner lest we be threatened by dumping, lower labor standards, and the collapse of our foreign markets.

American labor standards must be protected from countries with low wages, long hours and subnormal working conditions. We cannot aggravate conditions in industries already enjoying tariff protection in which there is constant technological progress and little economic stability. We must associate our foreign trade policies with a deliberate program to increase the purchasing power of our people. By expanding our own economy and improving the lot of labor we will not only set up standards which will guide the rest of the world, but also will be expanding both our capacity to absorb foreign products and the possibilities for foreign sales. An effective and constructive policy for international trade basically must stem from a stable and advancing national economy in which the problems of unemployment are successfully resolved.

Remarks by the Chairman

President Mitchell: The last speaker on the formal program is Mr. Charles F. Darlington, Foreign Exchange Manager of the General Motors Overseas Operations. His topic is "The Conduct of Foreign Trade under the Trade Agreements". Mr. Darlington!

THE CONDUCT OF FOREIGN TRADE UNDER THE TRADE AGREEMENTS

CHARLES F. DARLINGTON
Foreign Exchange Manager, General Motors Overseas Operations

MY share in today's program is to tell you something from actual experience in conducting foreign trade under the trade agreements, and to give you an idea of the significance of these agreements as viewed from a position in a company which has a large domestic as well as foreign business. At the outset I must utter this word of caution—that not everyone in exporting businesses, or even in my own business, sees the trade agreements through the same eyes—so I will have to ask you for your own protection to take what I say as simply the expression of my own opinions, although I know that they are shared by many.

What Limits Export Sales?

First, a word as to how our business is conducted. General Motors Overseas Operations exports the Corporation's products, chiefly passenger cars, trucks, and Frigidaires, from the United States to almost every country. I say " almost "—and here we at once have to mention trade restrictions, for in some countries our products are entirely excluded by tariffs or other measures, but I believe that we operate in every territory on the earth from which we are not barred by the government.

If we could sell throughout the world to any individual who wanted to buy a Chevrolet or a Buick or some other of the Corporation's products, and who had money to pay for it, as we can here in the United States, what an immense foreign market we would have! Ours and other American cars please consumers everywhere, and like so many typical American goods, almost do they sell themselves through their quality, attractiveness and moderate price. The limitation on sales abroad is not so much that of the purchaser's pocketbook as it is of the various national pocketbooks. Hence it occurs not at the customer's door but at the national frontiers. That is the point of limitation.

The great majority of import restrictions, particularly those affecting our products, are not imposed for protection of local industries; and, while customs duties in some cases have revenue as their object, even this reason is lacking in the cases of import quotas and exchange controls which are the two most effective devices of restriction. Why then do governments have resort to these measures? Needless to say, it is not out of caprice, for, generally speaking, they would be only too glad to allow their people to buy and enjoy more American cars and other imported goods. The difficulty of obtaining dollars—the exchange difficulty — is the basic factor which dictates their action. Certainly as far as our business is concerned — and this is generally true of all American export businesses—the international payment problem is the bottle neck of foreign trade.

There are many cases, of course, where trade restrictions are unjustified, and doubtless if I searched our files, I would discover instances where they have been applied with excessive severity or possibly in a discriminatory manner against us. But by and large we must admit that foreign governments have little choice when they limit imports of our goods. They cannot permit their country to buy more than it can pay for, for theirs is the responsibility of maintaining the national currency and of preventing the nation's reserves of gold and other foreign assets from being dissipated. Under the international monetary system existing before the World War, adjustments would have occurred in the price structure, and imports would have been limited more or less automatically to the nation's capacity to pay. Now the same function is performed under government guidance by tariffs, quotas and exchange restrictions.

The efforts of governments to limit purchases from the United States to what can be paid for cut into our sales possibilities in several ways. First, the foreign market is reduced in total. The potential purchasers who go unsatisfied do not realize that import restrictions are the cause of this, for, with the supply of cars limited, those that are admitted will be sold at higher prices, and the marginal purchasers will believe that they are withdrawing from the market voluntarily. Second, a part of the total quota, and perhaps a large part, may be given to other exporting countries to which it is easier to make

payment than to the United States, even though it may be American cars that consumers would have preferred; and finally, an increasing amount of manufacture must be performed locally.

More frequently than not these measures are uneconomic, as the governments imposing them often readily admit. But in a world as disordered as that of the nineteen-thirties, only the very few, economically strongest nations have been in a position to take constructive action, and of these, we have been the outstanding one. The great majority have had to bend to events, turning themselves as best they could.

What Has Been Accomplished Through the Trade Agreements?

Into this situation the United States came with the trade agreements. Not infrequently I hear the charge that the program has failed to accomplish much in the way of practical results, but with this I differ emphatically. When the circumstances in which the agreements have been negotiated are fairly considered, their achievement must be recognized as surprising and, as far as the British and Canadian agreements are concerned, spectacular.

At home the nation, traditionally protectionist, was passing through a phase of pronounced isolation, a circumstance which appears to have necessitated greater caution in granting concessions than even a conservative appraisal of the economics in many instances called for. Another difficulty has been that, although our market provided much inducement, our tariff rates had been raised to such extreme levels that even large reductions often held little promise to the other countries of appreciable trade increases. Our government's bargaining power with most countries, therefore, has been relatively limited.

Abroad the difficulties of the time have been even more obvious. The entire life of the trade agreements program has been lived in years of unprecedented economic nationalism. To expect that our lone efforts could have reversed this tide, running in its full flood, is unreasonable. There can be no doubt, however, but that the condition of world economic life was, up to the outbreak of the war, and is even today, healthier by far than it would have been had this country not pursued

the trade agreements program. The fact that the United States, the most powerful force in the world politically and economically, stood up for trade under liberal principles and equality of treatment through these dark years is a fact in world history of the utmost importance. I do not propose to try to tell you how much worse international economic relations might have become had the United States not taken this stand, but my considered opinion is that the difference would have been appalling.

As far as our business is concerned, better treatment for our products has been obtained in a number of countries, and our most notable increases in exports in recent years have been with these countries. Taking the automotive industry as a whole, exports which had amounted to almost 735,000 cars and trucks in 1929, and had declined to 120,000 in 1932, a loss of 84 per cent, had recovered to 475,000 in 1937. Even in 1939, despite the war, exports were 260 per cent over 1932. The industry does not attribute this entire gain to the trade agreements alone, but it is convinced that they have been a most important factor.

The essential point to be borne always in mind is that nations must be able to sell if they are to be able to buy. Nowhere is one made more keenly aware of the intimacy of this relationship between exports and imports than in the job of handling foreign exchange for an exporting company. The United States is practically the only nation that does not face a constant struggle to find the foreign coin to pay for the goods its people must and want to buy from abroad. The devices to which numerous others resort show the difficulty they have with their international receipts and payments in making ends meet. More than one nation, for instance, has asked us to accept deferred payment in notes. Another sells its principal crop in the autumn and has to wait until then to pay most of its year's bills. And time and again, if the exports of a certain country happen to increase a bit over expectations, or if the prices of the commodities in question rise, we find an almost immediate reflection in the amount of exchange that we can obtain and hence in the number of cars we can profitably send to that market. It is obvious that anything which makes it easier for foreign countries to sell their goods to us and obtain more dollars makes it easier for us to sell our goods to

them. Our gold policy, and the silver purchase program, have been and are methods of doing just this, but I must confess that I like the trade agreements better! We get more useful things in return for the things we sell!

The Importance of the Unconditional Most Favored Nation Policy

Of the various aspects of the trade agreements, none, to my mind, compares in importance with the unconditional most favored nation policy. It has, I know, many unfriendly critics, but the interesting thing about them is that in six years, they have been able to make so little of their case. The reason for this, I think, is that when the policy is closely studied, one is forced to the conclusion that it has no practical alternative.

If we do not treat other nations equally in our market, but instead give preferences to some and discriminate correspondingly against others, we must expect that our exports will be treated in the same manner. The negotiation of trade agreements would then become a matter of exclusive bilateral bargaining, which means nothing more or less than fighting all over the world for scraps of trade on a tooth-and-claw basis.

It is perfectly possible to enter into trade agreements of this sort; Germany and Italy have concluded any number and have made the securing of forced preferences the main characteristic of their commercial policy. Nor have the totalitarian states been alone in this. Great Britain, while not entering into strictly bilateral arrangements, has incorporated bilateralistic features in many of its agreements. Our position, however, is particularly unsuited to such tactics, for we have an export surplus in total and with most of the countries individually. How can we—a nation of 130 million people—approach another nation which, although only a fraction our size, may be buying from us two or three times the amount we are buying from it, and attempt to coerce it to give our goods still better treatment? Such an attitude, although often advocated in the name of realism, would be utterly unrealistic. The policy of treating equally all countries which are not discriminating against you is the best commercial policy for any nation, but for a nation which already sells in practically all countries more than it buys, it is the only possible policy.

There are some who will reply to this: "Oh, we do not advocate bilateral bargaining; we do not want to go that far; we are for the most favored nation policy, but feel that it should not be adhered to as rigidly as we are now doing." That attitude may be excellent in theory, but in practice it is meaningless. There is no half-way house; either you give and receive equal treatment or you give and receive preferences and discrimination. This is not to say that no room exists for latitude in the administration of the policy, but I am at a loss to know in what direction such latitude might usefully be exercised. On one hand are people who say that the policy should be enforced more vigorously and punitively against countries which in one way or another may still be discriminating against us; and on the other hand are those who advocate a greater willingness to recognize the validity of the preferential arrangements underlying this discrimination. With critics on both sides, one may conclude that the policy's administration has probably not been far from the middle of the road.

Should our government alter its policy and attempt to obtain preferences in foreign markets, I believe that the automotive industry would protest, for preferences in some countries would inevitably involve discrimination against American goods in others, and automotive products being an outstanding American export might well be the goods against which the discrimination was directed. Our industry does not want preferences because it does not shrink from fair competition, but it does fear discrimination, for against discrimination the best products and the most efficient organization cannot prevail. What our country desires is an equal opportunity with all others. We have no doubt that, given such conditions, we will be able to sell more automobiles than under any set of preferential arrangements that the United States could possibly negotiate.

The World in Which We Must Do Business in the Future

While the war lasts, exporters must live on a day-to-day, opportunist basis. Particularly is this true of the exporters of such goods as private passenger cars which use much-needed foreign exchange to buy and much-needed gasoline to operate. The war for us is a great misfortune. But not for us alone:

viewed in any but the most temporary light, it is a great misfortune for all American exporters and for American business generally. While it lasts, I do not expect there will be many new trade agreements. The main usefulness of the program through this period will be in preventing action prejudicial to our trade. The governments of all of the belligerent countries now have complete control of foreign commerce, and the things which under pressure of war they see fit to do, or to oblige their supplying countries to do, may often ride hard over our country's interests. In this situation our interests need increased defense, the armament for which is provided by our existing trade agreements and the Trade Agreements Act.

After the war, what will happen to our business and to the nation's foreign trade as a whole will depend primarily upon the character of the next peace treaties and of the type of world order that is built after them. This general question is much in the minds of business executives today. Business must constantly be studying the future, and the larger and more complex a business is, the farther ahead must it look and lay its plans. While you are purchasing Pontiacs, La Salles and Buicks of the 1940 model, our engineers are working on the models not only of 1941 but of 1942 and 1943. In the export field, we also must be thinking of 1942 and 1943 and even farther ahead, and be asking ourselves in what kind of a world we will have to work when those years come.

Whether the United States participates in the peace treaties or not, the importance of its practicing at that time a liberal commercial policy based upon the principle of equality of opportunity cannot be overestimated. After the war, Europe and Asia and most of the British dominions will have disrupted productive systems and peoples loaded down with debt. Their reconstruction will require an expanding volume of international trade and the resumption by the United States of large-scale foreign lending. This latter may sound distasteful to many, but it is essential. Our problem will be not how to avoid foreign lending but how to create the conditions in which it can be done beneficially and successfully. Primarily necessary to this is that confidence be reëstablished in the viability of the international economic order, which means that world trade must again be placed on a fair and equitable basis

and be conducted according to the rules of economics and not of politics. It seems not too much to suggest that the trade agreements may prove the cornerstone upon which the post-war economic reconstruction will be built.

The gold problem is one aspect of the reconstruction that is most important for the United States and for American business. My thought is not of the possibilities of inflation inherent in our large gold reserves, for these can be taken care of fairly well by action which is within the power of our monetary authorities and of Congress to adopt, but of the more fundamental question of the redistribution of gold which is necessary alike for us and for the rest of the world. If the international situation had righted itself without war, we might have expected that much of our surplus gold would have been withdrawn as foreigners repatriated their capital, but now this capital is being transferred to us for the purchase of war supplies and will no longer be in their hands when the war ends. Nor can we look for some time to come for any substantial redistribution of gold through the United States acquiring an import balance, even granting prosperity in this country. Inevitably the conclusion is forced that a resumption of large-scale foreign lending by the United States is the only way out.

Such lending is to me inconceivable if international commerce in the coming post-war era is to resemble that of the past decade, throttled and distorted by every conceivable device. So long as stronger nations make a practice of forcing preferential treatment from the weaker, and the conditions of foreign commerce are governed largely by political considerations, the confidence necessary for foreign lending will be lacking. And so long as imports into every nation are rigidly restricted by high tariffs, quotas and exchange controls, it will be impossible for the volume of international commerce to increase in a measure necessary to support the desired transfers.

The task of those who will sit at the next peace table will be to lay the basis of an order free of these faults. Whether or not the United States participates, its influence will be immense, and the pattern of the post-war world will probably be determined more by the policies it is following than by any other single factor. Preparation for that time, and, when it comes, the effective utilization of our strength in the true in-

terest of democratic civilization, constitute the most important tasks facing this country in the next four years. Nothing on the horizon can compare with them in significance to American business.

What would be the prospect of other nations adopting policies favorable to the expansion of world trade if by the close of the war the United States had relapsed into Smoot-Hawley-ism? What would be the prospect for world economic reconstruction if by then this country had joined the camp of those conducting their commercial relations on a strictly bilateral basis, forcing exclusive advantages from weaker neighbors, dealing in preferences and discriminations? What would be the prospect for the reconstruction of an international monetary system if we, with the bulk of the world's gold, were pursuing policies of political and economic nationalism?

There would be no more certain way than by the pursuit of such policies, I can assure you, of rendering our 18 billion dollars of gold history's greatest financial loss. After the previous war the United States made the mistake of loaning with the one hand and restricting international trade with the other, an unfortunate combination of policies which has led to the near-embargo on foreign lending imposed by the Johnson Act. But the Johnson Act did not do away with the problem, for we have it again today, different only in form. During and after the last war, we took bonds in payment of our goods; now we are taking gold. There is really no essential difference; the former bore interest coupons, the latter has more apparent security, but its worth rests upon its ultimate redemption in consumable goods. The ability and willingness of foreign nations so to redeem it depend essentially on our own actions, just as their ability and willingness to redeem their loans after the last war depended primarily on our actions then.

If after this war our national policies are to serve our true interests, it is essential that our government be pursuing, not half-heartedly but with vigor, a policy of trade liberalization based on the unconditional most favored nation principle. For this reason, as a Republican, I am profoundly disturbed by the attitude displayed last week by the Republican members of the Senate. Theirs was a most short-sighted stand for the senior members of the party which proclaims that it is, as it should be, the champion of business. Continuance of the trade agree-

ments is one of the most important long-range requirements of American business today.

I have stressed the international aspects of the trade agreements in their relation to business, but the international and domestic aspects at heart are one. To the development of conditions here in the United States the trade agreements, and particularly their conduct under the unconditional most favored nation policy, have the greatest significance. Domestic conditions are continually influenced by the agreements through the increased exports they make possible, and more importantly through the savings to consumers which result from the lessening of the price rigidities supported by tariffs, and the strengthening of our economic body by the substitution of strong production for weak. These deserve mention, but the thought with which I wish to close concerns something more fundamental.

Unless its character and organization are to be radically changed, American business requires the continuance, if not the reinforcing, of certain conditions in this country. Above all it demands the preservation of democracy and, with the political form, the maintenance of our personal liberties, and of individual initiative under the minimum of essential restrictions. It requires, moreover, the preservation of the system of private capitalism which, being private, is the only type of economic organization under which men in the modern world can enjoy personal freedom. Hence an excessive centralization of power in government—and the substitution which inevitably accompanies such centralization, of government by men for that by rules—must be avoided.

Experience shows, and reason indicates as well, that these values cannot be preserved in a nation that is isolationist and nationalist. In such a state individual freedom inevitably becomes increasingly circumscribed. You cannot confine the system of private capitalism, the democratic system, in watertight compartments and expect it to survive. It requires a world in which nations, as well as men, live under law, and where barriers to the expansion of commerce are as few as possible. If this system is to be preserved, upon which modern business as we know it rests, our country must steer wide of the paths of political and economic nationalism and must follow policies of the nature of which the trade agreements provide an inspiring example.

DISCUSSION: RECIPROCAL TRADE AGREEMENTS: POLICY, PRACTICE AND PURPOSES

CHAIRMAN MITCHELL: Discussion under the ten-minute rule will be conducted by Professor F. A. Southard, Jr., of Cornell University.

PROFESSOR F. A. SOUTHARD, JR.: About this time, naturally, ladies and gentlemen, any audience would wish that it could begin doing the talking. I will endeavor at least to play the rôle of one who, although sitting on the platform, is trying to discuss the papers we have just heard.

Professor Schumpeter gave us a hint which later, in another way, was developed by Mr. Rieve. Professor Schumpeter, you recall, indicated that as long as there was not full employment, the difficulties of any sort of tariff adjustment which the export industries would like—in other words, the sort of adjustment admitting imports and hence possibly gaining us foreign concessions—are greatly intensified.

Mr. Rieve, speaking for the textile workers, went further and said that his industry does not believe that there is any real likelihood, certainly no real assurance, that the expansion of the export industries (assuming they expand through concessions of one sort or another, possibly striking the textile workers) would provide the sort of reëmployment that naturally enough any capitalistic group or wage-earning group would seek.

Well, there is the issue; and if any of you in the last few days had read through page after page of hearings of the Committee on Ways and Means, as I have been doing, I think you would be impressed with the fact that we have here no new issues. I am sure you could go back to the tariff hearings of 1930, or of 1922, or of 1913, or of 1909, and find the same basic controversy, the protectionist groups coming before the Congress, or its Committees, and insisting that certainly there was no sense in admitting into this country products already being produced here at the obvious expense, or at least the probable expense or the possible expense, of the workers and of the investors in these protected industries in this country. Certainly agriculture, even Mr. O'Neal's group, has qualified its approval—in so far as agriculture has approved the trade agreements program—by the proviso that imports that are competitive should not be allowed to enter at the expense of so-called parity prices.

Within the country, within our territorial limits, this everlasting problem in a changing economy of what you are going to do with industries, that are losing out in the face of new industries or products, is one for which there is simply no solution short of prohibiting or restraining new developments. The textile industry of New England has found it exceedingly difficult to meet the new conditions in the South, resulting from the partial migration of the industry to that part of the world. We are seeing trade barriers develop between our states, but thus far we still are prepared to face the fact that when the workers or the investors in an industry, however long established, find that a new product is winning popular support, or a new competitor has a lower price or a new policy, there is simply nothing to be done about it. We have accepted that. Hence it is a curious thing, is it not, that when someone suggests that it might be desirable for the sake of a fairly efficient part of the economy to expand the trading area to another but exterior purchasing group—in Argentina, or elsewhere the suggestion strikes people as being quite different theoretically and fundamentally from the situation which, as I said, exists within any country.

I suppose that Mr. Rieve would reply that there is this difference, that as long as the competition that the textile worker faces comes from within the United States, whether within a new part of our textile industry or whether from some quite different industry, it is at least competition within a broad area in which there may be, and at present is, some effort to attain state-wide or region-wide or nation-wide standards of either wages or hours. I grant that if a country such as ours is trying through collective action to decrease hours and put a bottom on wages, and if we are doing that more rapidly than other countries, there is a problem created that the tariff maker must consider, however much he may be committed to the idea that we must expand as rapidly as possible the outlet for export industries. But I wonder if it is not appropriate to point out that we certainly slow up whatever process of adjustment in other parts of the world is raising their labor standards, if we are going to make them wait for their access to this market until their labor standards are as good as ours. One reason foreign labor standards are probably not as good as ours is that they are obliged, partly because of inadequate access to markets for their products, to trade on a plethora of labor and a plethora of almost nothing else.

Despite the fact that we admittedly do not have full employment, and that we therefore find it difficult to suppose that there will be immediate reëmployment following tariff adjustments, such as you might find in a country or an economy fortunate at all times to have full employment, may it not still be possible to find certain areas

in the world that are only too eager to accept our goods in considerably increased amounts, provided, as Mr. Darlington said, we can assure them the source of dollar exchange they need? In Argentina, for example, these two things fit together immediately. There is an almost immediate response, in their imports of our goods or of goods of the world in general, to the export of their own products. If there can be an assured market, an assured expansion in automobiles, in airplanes, in certain agricultural products such as citrus fruits, and so on, and in office equipment, and all the rest of our export products, then certainly one would suppose that we could expect increased employment in these industries.

I have used up my minutes. I am only trying to express my own feeling that it is not essential, in either practice or theory, for us to believe that the lack of full employment and the existence of rapid industrial changes and varying wage standards throughout the world close the door to any sort of effort to salvage the more effective high wage industries in the country, even if it does necessarily mean that there will be people, in the protected industries that receive less protection, who will be thrown out of employment. I am quite prepared, as far as Mr. Rieve's paper is concerned, to say that if I had to believe that there was no prospect of reëmployment, certainly I would see no excuse at all for trying to reduce tariffs. Secretary Hull's assurances seem to me to be assurances based on the only propositions that one can believe in here: that it is no mere accident that the export industries pay the high wages in the country, and that the protected industries, as a group, pay the low wages. I must confess that I cannot quite see the direction in which an economy is moving that is obliged to have its economic foreign policy dictated by the low wage industries.

CHAIRMAN MITCHELL: Professor Southard's remarks complete the formal program. We have a brief time left for discussion from the floor under the five-minute rule.

MR. OLIVER WILLIAMS: I should like to ask a question of Mr. Rieve. Did he not make an error in discussing price levels and wage levels?

In the first place, the assumption was made that the price of a good has something to do with the cost of its production. I think that is erroneous. I do not think that the price of merchandise has anything to do directly with its cost of production. For instance, if Japan can make five automobiles a year, and America can make five million, the cost of production of those five automobiles will not affect the price of world automobiles at all. If a country like Japan produces textiles cheaper it does not necessarily affect the world price of textiles if at the

same time other factors increase world purchasing power for these goods.

It seems to me that the important point to remember is that price is a matter of supply and demand and not of the cost of a part of the supply.

Furthermore, regarding competition between machine industries, a country like Japan would not normally expand along these lines. But if we refuse to accept Japan's handwork products, like toys and painted chinaware, we make her economic conditions abnormal. For example, if one were to invest $10,000 in Japanese industry it would be natural to take into consideration Japan's advantage of lower-wage skilled labor and not put the capital into automatic looms and similar machinery.

Instead of asking for a limitation of the world supply of textiles we might do well to consider how to set free the world demand, by such measures as permitting Cuba and Argentina to exchange freely their sugar and linseed for American textiles.

Conversely, this would lower the cost of living for American textile workers and in so far raise their real wages.

A wage scale is not a prevailing wage, if it is accompanied by great unemployment. A lower wage might result in more production, lower priced goods, and more abundance. For that reason a wage comparison between America and Japan can be very misleading.

We may find that the way to increase wages is not to restrict the *supply* of working labor by force and by law, but to heighten the *demand* for men by permitting naturally profitable industries from cotton farming to automobile manufacturing, to enlist idle capital for expansion in world trade.

Chairman Mitchell: Do you wish to reply, Mr. Rieve?

Mr. Rieve: I think different industries, probably in different products, would be affected differently. The basic raw material of textiles, either cotton or wool, has a uniform price because it is bought in the world markets. Machines are almost uniform in scope. Overhead, of course, may somewhat differ; but you do eliminate the basic cost elements that may fluctuate, so that the only other element is the element of labor.

We are not speaking here of handmade products. If Japan, for instance, exports to America a little hand-painted china, that is one thing; but if the country exports machine-made, manufactured goods, that is an altogether different situation. I do not know whether it is generally realized, for instance, that in spite of the fact that Japan is the largest and almost the only producer of raw silk, she is

beginning to export more synthetic yarns to this country than any other country.

Japan is becoming industrialized, yet we cannot even mention wages. I mean, in particular, wages in the textile industry. What they still have in Japan is the old method of apprenticeship where, for instance, girls are taken into dormitories and are signed over by their parents for three or four years. The company keeps them in dormitories, supplies them with food and clothing and shelter, but offers no pay until the end of that three- or four-year period. Then the company gives them a few dollars as a dowry.

We have that type of thing to consider, and with it we must compete.

Now, in a highly competitive industry, while volume may or may not mean anything, if a sufficient volume comes in, even though it may be negligible as far as the total product of the industry is concerned, whatever price is established for that little volume automatically becomes the price on the market, because, in an industry that is overdeveloped and is trying to fight for a market, prices are bound to be reduced in order to meet competition. Of course, the easiest way to reduce price is to take it out of the hide of labor.

MR. LOWELL H. BROWN: I would like to call attention to the latter part of the remarks of Mr. Darlington, which I consider to be a more important contribution than the balance of the discussion on the effect of the trade agreements.

The trade agreements in the present international economic situation have been like erecting a barbed wire fence to stop a flood. Judging from the past three months, the effect of economic nationalism, in the international situation which exists today, has been to increase exports for the year to a total of nearly four and a half billion dollars, almost $1,300,000,000 more than in 1939, directly as a result of the war.

The pound sterling in August was about $4.07; today the pound sterling is about $3.50. The trade agreements have had no effect on these statistics. Imports into Great Britain in the middle of 1939 were at a rate of about 50,000,000 pounds sterling. Imports into Great Britain at the present time are at the rate of about 100,000,000 pounds sterling.

Now, it does not take very much detailed study to realize that the fundamental defects of the economic situation today are not in these minor matters which have been given so much attention. As Mr. Darlington said, the major question is whether or not a new international order of some sort will result from the peace.

MR. NOEL BEDDOW: I was very much interested in the remarks just made regarding the total exports and imports to the United States of America. I come from a part of the country which, in the apt phrase of the President, has been called the part that is ill-housed, ill-clothed and very poorly fed.

Mr. Brown is right in his references to the total amount of exports and imports, but he forgets that exports, as Mr. Darlington has stated, may be increased under certain conditions, and that exports recently have been increased primarily because of the war. Too often we fail to take into consideration the fact that we are now exporting manufactured goods, and that the United States of America is not only a manufacturing country but an agricultural country. In manufacturing goods for export we are employing labor; we are employing labor in the automobile industry, for example, that is paid well for what it does; and if we can continue to export manufactured goods (I detest the export of materials for mass murder), whether it be in the textile industry, machinery, or what not, we are going to put more money into the hands of the American people so that they can buy the products of the farmer.

I am for the farmer 100 per cent. I am in favor of these reciprocal trade agreements. I believe they are one step forward, one way to help us out of our difficulties today.

MR. GEORGE CLARKE COX: I simply want to point out in connection with what Mr. Darlington has said, that we are going to continue to have the condition which gives us two thirds of the world's gold, either in more gold or in cash, if we do not allow people to sell us proportionately what we sell to them. I do not think this needs any elaboration whatever.

My point is only this: If we keep on selling more than we can accept, and counting it a virtue to do so, we shall not only get all the gold, but we shall get a lot of I.O.U.'s in addition.

The way to prevent this is not easy to find. I believe that the reciprocal trade agreements represent one way. They need changing in many respects, but they are a beginning.

CHAIRMAN MITCHELL: Is there another question?

MRS. ROY NICHOLS: Does General Motors have the figures as to the extent to which the export of its products has been directly assisted by the silver purchases, or the gold purchases?

MR. DARLINGTON: No; such figures, I think, would be quite unobtainable. Nevertheless, one may certainly say that our exports would have been less had it not been for the silver purchases, and would have been very much less had it not been for the gold purchases.

MRS. NICHOLS: Where have the silver purchases appreciably increased the export volume?

MR. DARLINGTON: I do not think it is necessary to point out any individual country. Of course, you can point to Mexico. We have quite a good market in Mexico, and the Mexican economy is largely supported by our government's purchases of silver; but I do not think that it is necessary to point to any individual country, because if you put dollars out in the world, the purchasing power flows everywhere. It is not necessarily canalized within the countries which receive those dollars. Does that answer your question? Mexico is the outstanding country; China, of course, also, and Spain and possibly Peru.

MRS. ALEXANDER HADDEN: Is there any group studying this economic question in the way that Mr. Darlington has proposed, so that there will be information available at the close of the war? I think that an educational campaign should be carried on among business men and many others to promote a better understanding of the trade agreements and the importance of our government acquiring larger reserves of essential war minerals that may be desperately needed, instead of more silver and gold.

Is there any group studying this problem from the point of view of the economic situation as a whole in order to evolve a constructive program, looking toward the next peace?

MR. DARLINGTON: I think that is a very good point. I do not know of any group that is devoting continuous study to it. Of course, a number of groups, such as this group here today, have it as the topic of their discussions. The education on this subject, of course, is being done chiefly by the Department of State and by other government agencies. Among private agencies the Foreign Policy Association and similar groups are giving out information constantly; but I do not know of any private group or agency devoting itself to what you might call a factual study of the program.

MR. SOUTHARD: I might mention the committee jointly chaired by Dr. James T. Shotwell and Dr. William A. Nielson who are trying to coördinate a very considerable amount of research on the nature of a durable peace.

CHAIRMAN MITCHELL: Mr. Grady, have you anything to add?

MR. GRADY: I have nothing to add, except that some of the women's organizations, like the League of Women Voters, the National Federation of Women's Clubs, and the Association of University Women, are now carrying on studies of this question.

MR. PETER L. XAVIER: I believe that the reciprocal trade agreements are so important that it is imperative to remove from our minds anything that may prejudice us against this very desirable program. After all the husks of political propaganda in the newspapers have been removed, there are two kernels of economic truth which might be counted against the reciprocal trade agreements, not in principle but in operation. I refer to the importation of Canadian wheat and the buying by the Navy, under a contract, of Argentine beef, after billions have been spent by the Department of Agriculture to reduce the production of wheat and beef.

It seems to me that the government should work as a unit in all of its departments. There should be no working at cross purposes. Since the State Department and the President have been given a new lease of authority, extending for three years (though the Senate did so by a margin of only three votes), it seems to me that this point should be cleared up. The Hearst newspapers and other journals have criticized the State Department, and more especially Congress, for not supporting the right of the Senate to ratify these trade agreements. Would the sectional interests of the farmers, the wheat farmers and the beef producers, be better protected by Congressional ratification than by executive control of these trade agreements? Perhaps some of the gentlemen here can clear up these points.

MR. O'NEAL: I sat in the gallery of Congress when they brought up the question of canned beef from Argentina, and I do not believe that I ever saw so much of a tempest in a teapot in my life. Now, I think, there is a law that you cannot use it any more.

MR. GRADY: In the Navy.

MR. O'NEAL: Of course, you New Yorkers and others can use corned beef. There is a heavy tariff on wheat. I did not say in my statement that farmers are always glad to see a little in the way of imports come in, because imports never come in at low prices. We did not have any imports of agricultural commodities at all when prices were sharply declining, and you in New York, and in the rest of the United States, were going to vote very fast because the farmers had no purchasing power.

Mr. Chairman, I would like to say one more word, if I may, concerning Mr. Darlington's magnificent statement. Do you not think that, as American people, we ought to emphasize in our statesmanship this fact, that we are able folks? I heard my good friend, the textile worker, talk a while ago about his textile industry. I raise the cotton down in Alabama, sell it to him for eight cents a pound. The people on the farms make about five to ten cents an hour, as a maximum; and he gets twenty-nine cents!

MR. RIEVE: Thirty-two and a half, in the South.

MR. O'NEAL: I know we tried to hold you down, because you were too damned high! But that is not the point; it is not the twenty-nine cents or the eight cents. With reference to the question which Mr. Grady answered, in one sense, the farmers are asking all their great educational institutions—and we have one in every state, Mr. Chairman—to make very careful studies of the trade treaties, just as I reported that Ames College in Iowa was studying it.

The farmer does not ask for twenty-nine cents; he does not ask for a dollar and a half for wheat. He does not ask for forty cents for eggs. He does not ask for thirty-five cents a pound for butter. All he asks for is the right to a fair exchange for his commodities. Parity does not mean a fixed price; it means a fair exchange of goods and services. I think that the vast majority of farmers in the United States are particularly anxious for the survival of the capitalistic system; but I am saying to you, frankly, that it cannot continue unless we put these millions of people to work.

The farmer is not insisting on twenty-nine cents, or forty cents, an hour. He is not saying that; but he is saying: "Let everybody go to work. Let's exchange our commodities. Let's use this gold. Let's use the great technological development of the greatest nation that God has ever made on earth. Let us, for the benefit of humanity, both in America and in the world, use what we have." And God knows I am not afraid of anybody, anywhere else. I think we ought to banish fear from our hearts. I told Mr. Treadway, of Massachusetts: "In the olden days, you sailed your ships from New England all over the world, and you spit in the eye of the other fellow. You fought a war, and now you're afraid; you're fragile in New England. You are weaklings."

I am not; as an American citizen, I am not, and I think we have to face in a statesmanlike way the position that God has given us in this world. We must not sit here saying, "Oh, I'm afraid, I'm afraid."

MR. LAWRENCE FRENCH: This is a matter which is related to the one which we have been discussing this morning, and I would give my most hearty approval to Mr. Darlington's remarks. It seems to me there is a link in the chain which may be in the minds of many of us; that is, the tremendous problem of refugees and of hungry people in Europe and in Asia as a result of these wars. If America is going to get the trade that should normally flow from the continuance of trade agreements, one of the steps will be to gain the good will of these people. It seems to me that one of our

major problems now, and in the months and years after the war is to help feed those starving people, and to help share in the care of the refugees.

CHAIRMAN MITCHELL: I must now declare the meeting closed.

PART II

TRADE BARRIERS AND WORLD PEACE

INTRODUCTION *

LEON FRASER, *Presiding*
President, The First National Bank of the City of New York
Trustee of The Academy of Political Science

IT is my privilege on behalf of the Trustees of the Academy to welcome you to this gathering.

For sixty years, now, the Academy has devoted its semi-annual sessions to the nonpartisan discussion of current problems of public affairs and of economic relationships, both domestic and foreign. Its publication, the *Political Science Quarterly*, has come to be known to scholars, and to be respected by them, wherever scholars are.

At this moment, when, even as we talk, tragic, dramatic and epochal events across the sea are shaking the world, shaping its and our history and making destiny, how incongruous, how impotent, how inappropriate it seems for us to be sitting here in satisfied comfort, abstractly debating in an academy, just as if on two sides of the globe mighty issues were not joined. One's first natural reaction is that we should fold up our talking tents and creep away.

Yet in these critical times, if we control our emotions and take second thought, and if we will but examine the topic of today's conferences, we shall recognize that the subject is very germane, philosophically speaking, to the struggle in the North Sea and on the Chinese plains. For is not one of the factors causing this world disturbance—I do not say the only factor—but is not one of the predominant factors precisely *economic nationalism, trade barriers and war?*

* Introductory Address of the Presiding Officer at the Second Session of the Semi-Annual Meeting.

These three dis-Graces go hand in hand, and always have. To give profound consideration to our public policies concerning them, even while a battle is raging, is really not so incongruous, so impotent, or so inappropriate as it first appears, any more than one should desist from inquiring into the fundamental causes of a plague while people are dying of it. Even in darkest hours, our minds look ahead, and the life spirit never dies. We unceasingly think of the world that we would like to see for America, and for mankind after this conflict shall be concluded.

Here, again, the subject and the policies of economic nationalism and trade barriers are of vital import. Will their further adoption, earnestly advocated in some conscientious quarters, make America more or less secure, more or less happy, more or less prosperous? And as America goes, so goes the world, for our influence is so great, our strength so dominant, that our policy, once clearly adopted and followed, is likely—nay, is certain—to be the guidepost for the remainder of the globe.

Rich in gold, shall we not buy extensively from abroad? Rich in productive capacity, shall we not produce and export to abroad? Rich in consuming power — a potentiality still hardly scraped—shall we not enjoy the good things of the earth and bring them to us from all the Seven Seas? On that route, I feel, lies the greatest likelihood of greatest satisfaction, and the most fruitful approach to the attainment of those more pacific relations that men have so long and so vainly sought. There are many who tell us that this is the wrong route, and that the beauties of it are mere idealism and phantasy. Perhaps the speakers today will throw light upon these weighty questions and help us select the proper course.

Of the two speakers, the first, who will speak on "American Policy: Positive or Negative?", is an educator, an historian, a particular student of foreign relations, the administrator of a great institution of learning in the Providence plantations! I take pleasure in introducing the President of Brown University, Dr. Henry M. Wriston! (Applause)

AMERICAN POLICY: POSITIVE OR NEGATIVE?

HENRY M. WRISTON
President of Brown University

THE world yearns for peace, but all too often talk about peace tends not to promote it but to manifest merely a flight from reality. Three such manifestations can be very briefly stated.

The first is the emphasis upon peace as something to be made in the future, "at the end of the war." That idea lulls the public to sleep when it needs to be vigilantly awake. Peace is not the product of the untrammeled thought of men at a conference table; it is a reflection of the habits of mind which have become dominant before and during the course of the war. The Treaty of Versailles, now so heartily condemned, was the product of aims, purposes, and habits of thought nurtured during four years of war. Similarly the recent peace imposed upon Finland represents only the specific act of realizing a policy long matured in Moscow. Just as the Constitutional Convention of 1787 crystallized out of habit and tradition and experience the substance of our governmental form and the structure of its powers, so the coming peace is now really in the making; its form is more plastic at this moment than it will be subsequently, but the elements of that peace are already being shaped. That is why it is a flight into unreality to suppose that the problem of peace may safely be left to the future. Our actions from day to day help shape it.

The second manifestation of unreality in thinking about peace consists in assigning responsibility for the peace exclusively to nations abroad. Men say "Europe and Asia are fighting; let Europe and Asia make the peace." But that is not the whole truth. Without taking up arms we assert our force in certain war areas, and deliberately refrain from such assertions of force in others. We are definitely working to shape peace in important respects, and neglecting to do so in others. It is transparent, for example, that the United States seeks to maintain the Chinese in a position to continue the

struggle with the object of preventing an unfavorable peace. We have refused to recognize Manchukuo; that is a positive act, the importance of which is recognized elsewhere more fully than here. In an oblique way the United States sought to stiffen and support Finnish resistance. The abdication of our neutral rights under international law profoundly affects the conduct of the war in Europe. The fact is that American interests are deeply involved in the existence of strife anywhere, and in the measures taken to end that strife. By direction and by indirection, sometimes more importantly and sometimes less importantly, sometimes positively and sometimes negatively, we participate in shaping both war and peace.

Neither Europe nor Asia can long maintain a peace of which the United States does not approve. The Treaty of Versailles furnishes all the evidence we need on that point. If we look at the history of the Far East during the last thirty years, we have another clear-cut illustration. So great is our weight in the balance of the world that we upset the balance not alone by throwing it toward one side or the other; jumping off the teeter board has an effect just as profound. This war is being fought in Europe, but those who say we have no responsibility for its inception, its course, and its consequences simply deceive themselves.

In the third place, unreality creeps in not only when we think of peace as remote in time and distant in space, but when we think of it as something on a piece of paper written by statesmen. This simply confuses form with substance. The leadership of statesmen is partly real, and partly an optical delusion by which we are persuaded that in following us they actually lead. They reflect our temper even more than they control it. Therefore, as individuals we cannot escape responsibility. We have no right to talk of peace unless we first ask what our own responsibility may be, whether we are in favor of policies that make for the kind cf world in which peace is possible.

I start, therefore, with the premise that peace is being shaped here and now, and to some extent by us—not alone by us, of course, but none the less importantly. In the light of that premise I want to examine briefly the central paradox in the world's search for peace: the attempt of nations to pursue simultaneously utterly contradictory policies.

We are advised in Scripture, when giving alms, not to let the left hand know what the right hand doeth. Often we act as though that were an admonition quite different—to have the left hand find out what the right is doing and checkmate it. When that happens in an individual, we speak of a split personality and recognize it as a dreadful calamity. Indeed, it often leads to suicide. The nations of the earth (including our own) exhibit that fatal defect—and war is in fact suicide.

Let us put this paradox in plainest terms: we do everything by engineering and invention, by ingenuity and technology, by courage and treasure to make commerce not only possible, but inevitable—to give it the greatest volume, the greatest mobility, the greatest freedom. Simultaneously we set up political barriers to hamper and defeat it. Is it any wonder that it is said we live in "a dark hour of a great age", or that Ortega y Gassett with acid clarity said: This is an epoch "superior to other times, [but] inferior to itself"; an age "strong, indeed, and at the same time uncertain of its destiny; proud of its strength and at the same time fearing it."

Let us look for a moment at this tragic paradox through historical perspective. The *De Monarchia* of Dante, written at the opening of the fourteenth century, is a magnificent summation of the medieval concept of the human race as a single, universal community founded and governed by God. "Mankind", he said, "is a whole with relation to certain parts, and is a part with relation to a certain whole. It is a whole, of course, with relation to particular kingdoms and nations . . . and it is a part with relation to the whole universe." In passionate language he poured out the yearning for that unity. But his words were uttered in an age when physical obstacles made the longed-for unity impossible. Science had not yet unleashed its miracles, engineering had not yet improved upon the skill of the ancients so that means of communication, methods of travel, and agencies of exchange could realize that unity.

Now the situation is reversed. Since it is possible to fly in eighteen hours from New York to San Francisco, we would expect the feat to be recognized as a manifestation of the unity of this nation, of its compactness, of the reality of a national market and a national ideal.

But remember the paradox! Do the states accept the implications of that magnificent achievement? Quite the contrary. Interstate barriers have been raised to the highest point in the history of this nation under the Constitution. A determined effort is being made to establish the equivalent of interstate tariffs. Having for a century and a half enjoyed the blessings of an enormous free trade area, having seen that policy and that practice weld together the interests of this nation, in the name of local patriotism men seek to destroy it.

We read in our histories of nullification in 1832 and thrill to Andrew Jackson's stirring toast, "Our Federal Union, it must be preserved." We know the poignant tragedy of Robert E. Lee who found himself in a dilemma of patriotism between his state and the United States. We had thought the war between the states had resolved for all time that dilemma, and effectively preserved the Union. Abraham Lincoln fulfilled the promise of Andrew Jackson. Yet today new nullificationists, not so frank, not so bold, stealthily, by devious devices, seek to destroy the constitutional guarantees against interstate barriers. Those guarantees were established when trade between the states was limited by distance, before means of communication and transportation made free interstate trade possible. But now that we have fulfilled the dream of making those boundaries meaningless by taking to the air, New York taxes the income of a flier who crosses the country for that portion of his flight which is over the soil of New York. Eight states of the Union have set armed guards along their boundaries and have established ports of entry like customs houses upon the borders of foreign countries. Some states have set up embargoes against the products of other states. No state has failed to pass some law calculated to destroy the national unity. An attempt is made to obey the letter of the Constitution but to defeat its purpose, destroy its meaning, and impoverish us all.

Similarly, in the international world, we are proud of the fact that it is possible to fly from this country to Europe in something under twenty-four hours, and we rejoiced only last week in the triumphant round trip of the Clipper in less than forty-eight hours. But we deny the implications of that magnificent act. International trade, facilitated by the miracles of transport, is obstructed by political action which has raised

the highest barriers ever established by nations to destroy their own prosperity. Autarchy is the strongest illustration.

During the centuries when men yearned for unity and developed a magnificent theory of a united world, the facts ran counter to their dreams. Now that there is the substance of a united world, we find ourselves with no theory, no instrumentality, and no faith that either can be created. Now that we have made the world a physical unity, now that we have made it literally a community of people, we reject any spiritual unity. We insist upon a supernationalism which does not permit us to love our own nation as a father and other nations as brothers and sisters, but demands that we love our nation to the exclusion of all others. The implication is that if we do not hate them, we cannot love our own. In human experience and in ethics, nothing is clearer than that a person cannot actually love anyone while he hates another. Yet that is precisely the demand implicit in the attitudes of many people in this country. Goethe's echo of Dante's great generalization, "above all nations is humanity", would today be regarded as a manifestation of active disloyalty not only in totalitarian states, but in many quarters in the United States.

Those who refuse to face the facts as to the kind of world we ourselves have helped to build, disguised as patriots, try to bully those who would discuss our obligations. They seek to inhibit the expression of moral judgments about the war, asserting that those who make such judgments are dragging the United States into active participation. The narrower and more provincial the nationalism, the more patriotic it conceives itself to be.

Those who would take care of themselves and let the rest of the world go hang yield to an impulse which has always been fatal to those who obeyed it. When Cain asked, "Am I my brother's keeper?", it was a dishonest question. No one has ever been deceived by Cain's question, unless he succeeded for a moment in deceiving himself. It is easy and specious to paraphrase Cain and say, "Let Europe solve its problems and we will solve ours." But that is also a dishonest effort to confuse the mind. For we helped make the modern world and cannot claim immunity from responsibility.

When Robert Fulton built the *Clermont* to ply the waters that wash the shores of this city, he launched a revolution in

transportation, which made it possible for America to send a million men to France and for the nations of the earth to burden the seas with their traffic. When Americans built the *Merrimac* and the *Monitor*, they altered the structure of sea power and laid upon the nations of the earth a tax for the building of navies beyond the wildest dreams of the imagination.

When the first message went over the Morse telegraph, "What hath God wrought?", its inventor might well have added, "And what have I wrought?" Similarly, when Alexander Graham Bell spoke for the first time over his telephone, he also altered the habits of the world and made it possible for men at a distance to confer as though they were in one room.

When Cyrus Field laid the Atlantic cable amidst the laughter of the skeptics, he created a tie between Europe and America that no wishful thinking can destroy. By that cable an American changed the future of Europe; the structure of the world was altered and we cannot slough off the responsibility.

A self-confident nation took over an abandoned ditch in the jungles of Central America and built the Panama Canal. Theodore Roosevelt had no doubt of the scope of its influence, for he said, "This . . . will, in its great and far-reaching effect, stand as among the very great conquests . . . won by any of the peoples of mankind." He was right, for it reoriented the trade routes of the world; it gave a new framework to naval strategy.

When Americans speeded up the industrial and the agricultural revolutions and developed the processes of mass production by automatic machinery, they profoundly altered the character of trade, reshaped the problem of raw material, affected the cost of goods, and revolutionized the distribution of benefits. They cannot now deny those achievements.

When Edison and his successors turned loose upon the world a flood of brilliance, and engineering caught the forces of electricity to harness them, power reënergized the implements of mankind in Europe as well as America.

When America took Marconi's invention and developed the technique of world-wide broadcasting, it gave to the spoken word the very speed of thought itself and language flashes

about the earth faster than a beam of light can be bent over its surface. The fact that it was done without appreciating all its consequences does not purge us of responsibility. Americans created an almost insoluble problem for the dictators and the censors of the world. For example, in the two weeks between the first and fifteenth of February, there were 131 radio programs received in one place in America from London, Paris, Berlin and Rome—58 from Berlin, 41 from London, 17 from Rome, and 15 from Paris. Twenty-seven programs were in languages other than English. They penetrated censorship as though it did not exist. Despite drastic penalties many of these broadcasts were heard by thousands in areas of Europe where listening is forbidden.

When the Wright brothers lifted their fragile power kite from the sands of Kitty Hawk, they changed the face of war, they changed the face of communication and of transport, they altered the habits of the earth. Now commerce is borne literally upon the wings of the wind. Their triumphs, exploited by their successors, have brought unforeseen but no less real and inescapable consequences for Europe and Asia, the islands of the seas, as well as for America. To pretend that our relationships are the same as they were before is to shut one's eyes to reality.

We have been, I am contending, the pioneers and the most effective single agency in the world for shrinking the earth upon which we live. Our forefathers were glad to flee Europe, but they were sorry that the barrier of the ocean was so great and sought to reduce it. They were glad to occupy this vast land, but they knew its political union depended upon physical union. Therefore, they turned their youthful energies with fierce zeal and rich ingenuity and magnificent courage to those tasks. No wonder Walt Whitman cried:

For we cannot tarry here,
We must march, my darlings, we must bear the brunt of danger,
We the youthful sinewy races, all the rest on us depend,
Pioneers! O pioneers!

I am not arguing that our achievements stand alone. We have traded not only in goods but in ideas. It is announced, for example, that synthetic rubber will be made in this coun-

try under German patents. Indeed many of the chemical marvels of our age are under German patents. No embargo, no blockade, no economic warfare can prevent the flight of that knowledge and its exploitation within our borders. As with synthetic rubber, so also plastics and thousands of other products have been worked out in the laboratories of the world and fly from one country to another with extraordinary speed.

Likewise, in the fight against disease, we do not and cannot stand alone. All are familiar with the miracles of sulfanilamide and its various derivatives. The fundamental work was done in Germany, but it was developed in France and England and its clinical use in America began at Johns Hopkins. Today many people are living who, without international scientific collaboration, would now be in their graves. I ask whether it is rational, whether it is intelligent for us to say that Europe be allowed to fall into such a state of decline as to set back its coöperation with us in the great battle against disease, in the exchange of ideas for scientific developments, in the promotion of the distribution of goods to the people of this earth.

Yet in the face of the triumphs of science and engineering, what is the temper of politics? Does it accept the responsibilities of these achievements? Does it implement intercommunication? Its temper can perhaps be illustrated by an amazing bill recently presented to the Senate of the United States. A statesman who has had the special benefits of heading the Temporary National Economic Committee introduced a bill designed to check the use of machinery, to put a premium upon hand labor, to penalize the one and subsidize the other. It was calculated to undo the industrial revolution, to withdraw from the workingman his radio, his car, his plumbing. It might better have come from someone sitting in a loin cloth, drinking goat's milk and spinning cotton. The Federal Communications Commission lays the dead hand of bureaucracy upon a scientific and commercial development, lest the product come to obsolescence. Must we now expect an edict from some government bureau against women's hats on the ground that they will be out of style next season, and must the costume jewelry business stagger into a decline because a beneficent government would permit us only those things which endure, like the pile of gold in Fort Knox?

The United States was not always in this timid mood in the face of its own achievements or before the world at large. Jefferson was thought to be a pacifist, and he had a dogma of "peace, commerce, honest friendship with all nations, entangling alliances with none," but he had no illusions about isolation. Although the Barbary pirates were Europe's problem and Europe was ready to pay tribute to them, he none the less sent our ships to the Mediterranean and cleaned up a nasty mess on behalf of the world, and freed commerce of shackles.

When we were weak and were told that events in Europe were of no concern to us, Daniel Webster wrote to Hülsemann, the Austrian Minister: "The power of this republic, at the present moment, is spread over a region, one of the richest and most fertile upon the globe, and of an extent in comparison with which the possessions of the House of Hapsburg are but a patch upon the earth's surface." The United States, he said, cannot "fail to cherish always a lively interest in the fortunes of nations struggling for institutions like our own." Words too bold for today!

It was a dramatic moment in history when a minor naval power sent an expedition half way round the earth to demand the opening of Japan. Commodore Perry changed the status of Asia, altered the balance of the world—and gave to trade fresh opportunities.

Despite the fact that the Kattegat and the Skagerrak were within the orbit of Europe in a very intimate and particular way (as the events of the last few days have illustrated), the United States did not hesitate to exert its influence for the abolition of the Sound dues in 1857—and helped break down another barrier to trade.

When the Far East was in a process of partition, at the end of the nineteenth century, it was an American Secretary of State who announced the policy of the "open door" and of the integrity of China with no squeamish hesitations because it was over the water. That was a reflection of our determination to keep open the channels of commerce.

If America had no hesitation in holding open the trade of the world at a time when trade had to surmount so many natural barriers, and before we could provide the physical facilities for it to surmount those barriers, how much more should we accept responsibility today when we are the most

powerful nation in the world and, more than any other nation, have made the world compact? Why should we run away from this reality? For reality it is. I am not suggesting we should assume the responsibility of others, but I insist we should accept the responsibilities we ourselves have created. Is it to be said that the United States is the first casualty in the "war of nerves"? Is it to be said that having been the most effective agent in destroying our isolation, we now cower in the presence of our own achievement? Is that the path to a peaceful world?

The bold, the vigorous, the decisive activities of the United States, both in science and technology and in commercial diplomacy, have not brought us to war, but to greater influence, a higher standard of living, and firmer prosperity. They have contributed to well-being and peace in the world. Whatever we may do by trade agreements or other political means to open the channels of trade is simply fulfilling our own destiny and contributing to peace upon earth. It will not do to have the right hand of science and technology pursue a positive course while the left hand of politics checkmates it by a negative course. Why not let the two hands work together to build a better world?

Remarks by the Chairman

Chairman Fraser: Trade barriers! The next speaker is a person who has no regard for trade barriers. After holding with distinction positions of distinction in the United States, we exported him to Canada — notice I did not say deported (laughter). And after holding in Canada with distinction a position of distinction, we re-imported him into the United States where he now presides over that splendid American institution, the Mutual Life Insurance Company of New York.

I present Lewis W. Douglas! (Applause)

EXTERNAL POLICY AND OUR INTERNAL PROBLEMS

LEWIS W. DOUGLAS
President, Mutual Life Insurance Company of New York
Vice-President of The Academy of Political Science

MAY I acknowledge my gratitude for the extraordinary and unmerited generosity which you have extended to me in your introduction. And then may I say that if my remarks today have been uttered by others—among them yourself, President Wriston—my only apology is that imitation is the sincerest form of flattery.

This session of the Academy is devoted to a discussion of the general subject, "Economic Nationalism, Trade Barriers and the War", and, in so far as the morning proceedings were concerned, to an elaboration of the effects of reciprocal trade agreements on various phases of our economic life.

I shall take the liberty of trespassing on the wider area, defined by the broad title, of which the trade agreements are but a small part. I shall do so because the agreements already made, and the authority to negotiate them in the future, are symbolic of an important principle of international behavior. They can be defined as a mechanism—an instrument—fashioned to effect, in the course of time, a freer flow of goods and services between nations. They are directed toward the mutual development of wider markets for the products of human effort. They were conceived to arrest, before war came, the dangerously rapid drift toward an intense nationalism which was proving to be—perhaps had already proved to be—what John Maynard Keynes so aptly called, "The serpent to this Paradise". If they arrived too late, it is not they that are to be condemned, but ourselves, for not acting sooner. Now that war has come, they serve the high purpose of extending the promise of better things, around which a new world may be reclaimed from the ravages of disillusionment and destruction.

May I say that in discussing the subject, there are three postulates which will serve as guides. Without inferring that the dead hand of what has gone before must fashion what is to be, the first is that, as Harrison put it in *The Meaning of History*, "all our hopes of the future depend on a sound understanding of the past." The second is that in political economy there are few, if any, absolutes and that the behavior of public and private instrumentalities may be both the cause of what slowly follows and the effect of what has preceded over an expanse of time. The third and final qualification is that political economy is not a subject divisible into isolated entities, and that any matter lying within its frontiers is but a segment of the whole territory it embraces. Hence, an analysis — limited as this necessarily is — of external commercial policy must be and, in fact, is related to internal events. The only appropriate basis for an examination and judgment of our foreign trade program is in terms of its consequences, its influences on our vital national interests. What is good for us is the only guide we should observe for our own conduct.

It seems to me appropriate to approach the subject of today's discussion by asking the question—"what has been our external commercial policy?" It has often been stated that the United States has pursued a policy of protection since the early days of the Republic. Is this an accurate statement? The evidence indicates that from the earliest days of our existence under the Constitution to the middle of the Civil War, taxes on imports were imposed for two purposes. First, to provide a mild amount of protection for what were called "infant industries" and, second, to raise revenue. Throughout the span of almost three quarters of a century of our early history, customs duties provided approximately 90 per cent of the income of the federal government. It was only during and after the Civil War that protection in a less mild, but still relatively temperate, form became imbedded in the public policy of this country. In the late nineties, the structure of the tariff schedules was once more changed. The rates were elevated and the mildness of protection, as it had theretofore been, became less mild. Indeed, rates began to be prohibitive.

Barring the Underwood Tariff Act of 1913, the trend from 1897 to 1934 was toward a greater degree of exclusion of more and more commodities. The movement reached its climax

in the post-war decade under the provisions of the Fordney-McCumber Act of 1923 and the Smoot-Hawley Act of 1930. Hence, since the Civil War, the drift here at home has been progressively toward the development of autarchy. I say autarchy because the word literally means self-sufficiency. As the restrictions on imports have increased in size, and the exclusion of foreign goods has become greater and greater, we have necessarily been attempting to develop, over larger and larger areas of our economic life, a system of production and distribution sufficient unto itself, and more and more independent of foreign commerce.

The issue today is, therefore, whether a policy aimed at economic nationalism—self-sufficiency—autarchy—creates an environment favorable to the reconstruction of a peaceful, tranquil, confident world; whether it encourages and fosters the employment of the unemployed. Experience and observation of brute fact may help us to provide strong presumptions, if not convincing answers to this question.

During that period extending from the Civil War to the end of the post-war period, certain serious maladjustments were being continuously produced in our internal economy. They existed in a particularly virulent form among those engaged in the unprotected enterprises as compared with those employed in the industries that were beneficiaries of a public subsidy. But the geographical frontiers capable of absorbing discontent (I would not infer that there are not now other frontiers challenging our creative abilities), still extending the promise of opportunity, concealed these maladjustments and obscured their full effects.

Moreover, because the United States, prior to the World War of 1914, was a debtor nation servicing its external obligations through the export of commodities which we were peculiarly qualified to produce, the manifold social consequences of what was a relatively temperate form of protection on world forces, as they impinged on our own interests, were never fully revealed or understood. When, during and after the first World War, our position was shifted from that of a debtor to a creditor country, other factors intervened to obscure for almost a decade the consequences of a commercial policy, which by then had assumed the proportions of extreme embargo protection. While the dislocations between the non-protected and

the protected enterprises became accentuated, the huge volume of foreign loans that were made throughout the period disguised the gathering forces of disaster. Although they temporarily financed the export of our surpluses, they were accumulating service charges on debts that could be met only by the importation of goods or of gold. It was only after the collapse came in 1929 that the seeds that had been sown throughout the preceding decade sprouted in fertile soil.

I would not be understood as minimizing the effects of the first World War—war expenditures, war-time inflation never fully liquidated, the unrealistic way in which the problem of reparations was treated, the post-war experience with depreciated currencies, in some countries decimating the middle class that had formerly given solid consideration to public questions—of strong national prejudices, and of a variety of acts taken to neutralize the social pressures aggravated, if not created, by the war. I would only say of them that our policy here supplemented the forces they engendered throughout the world.

As a creditor country, we refused, under the sanction of public law, to permit the servicing of debts and the purchase of our exports by the importation of goods. Throughout the entire post-war period, therefore, gold flowed steadily westward across the Atlantic, depleting, in relation to their liabilities, the stocks which were supporting the currencies of the European countries. Because the pound sterling was a currency used throughout a very large area of the world's surface and was the currency in which prices of world commodities were measured, its movement was of peculiar importance to our own interests. When the strain imposed on sterling by our tariff policy was intensified by the disintegration of the fabric of European credit, England at last abandoned gold payments in September 1931.

The depression, which before had been in the nature of a cyclical one, immediately became secular in character. What before had been not unlike many previous depressions became thereafter unique in modern history. The intensity of the deflation increased at home. It was reflected in a further precipitate decline in all prices and all values. Agriculture, if seriously damaged before, became almost completely bankrupt. Unemployment rose to an alarming, indeed a frightening,

figure. This resounding crash of values and this shrinkage of production finally culminated in the bank moratorium. On the record, it cannot be successfully denied that the abandonment of gold by England in the fall of 1931 increased the intensity of the depression at home to such an extent that socially it became almost unbearable. Certainly it created an impressive array of strains and stresses within our own economy that demanded consideration, and led to elaborate devices designed to relieve their tension.

The agricultural policy, payments to agriculturists for not producing, public loans conceived to support a certain level of prices and values, the policy of restricting production, were all aimed at abating the pressure so substantially augmented by the depreciation of sterling. To minimize further the distress intensified by the fall in the value of the pound, we at last ourselves abondoned gold and accepted, however unwillingly, a managed currency. To provide relief for the immense army of unemployed, we embarked upon a policy of huge expenditures. They, themselves, created such a host of vested interests that the spending, at first undertaken as a matter of relief, shortly became rationalized into what appeared to many, and still appears to some, to be quaint theories justifying an unrestrained use of the public credit. The doctrine of artificially increasing consuming power can be said to be a general summation of them all.

On the basis of experience, it is therefore suggested that the policy of extreme protection, aimed at self-sufficiency, pursued in its most aggravated form by the United States during the post-war decade, cannot be divorced from the extraordinary phenomena that we have witnessed during the course of the last nine years.

The intricate mechanisms created to deal with the situation have had two fundamental effects on our structure of government. First, they made necessary a concentration of power in Washington, which would have been considered fantastic except in times of war. Secondly, the administration of the various relief schemes presented such technical and intricate problems that the responsible representatives of the people, the members of Congress, were unable to cope with them and, hence, were persuaded to commit them to politically irresponsible bodies, and to delegate to those bodies extraordinary

powers to spend, to tax, to establish arbitrary rules and regulations which assumed all of the force of law.

It may be urged that, under any circumstances, the complicated nature of our society would have made necessary the establishment of administrative agencies clothed with broad powers, but it cannot be urged that they would have existed in such an accentuated form, vested with such vast powers, had the social strains and stresses within our country not been so tremendously increased by the abandonment of gold by England. Some may suggest that another administration might have resisted more successfully the demands of a distressed people, but this is not material to our discussion today. Some may argue that the problems might have been attacked by a direct frontal assault, or at least by a different flanking movement, without producing the results with which we are now burdened. But this, too, is immaterial to the present deliberation.

The fact is that the pressures were monumental and that the government undertook to reduce their tension by creating a series of intricate, unstable instruments vested with broad and relatively unrestrained authority. These are but a few of the fatal consequences of economic nationalism.

The policy of prohibiting the importation of a large number of foreign products, pursued here at home, was imitated, partly perhaps because of our actions, by most countries of Western Europe—indeed, by most countries of the world. It was ultimately reinforced by a long array of additional restrictive measures. The significance thus attached to the national frontier made it impossible for nations not generously endowed with natural resources to purchase their requirements in the world markets with the products of their effort. Hence their only recourse, the only method they could employ by which they could make available to themselves the materials which they needed to support their national life on a reasonable level of subsistence, was to push their frontiers out, first by diplomatic maneuvers and at last by resort to arms.

There is a curious and interesting parallel in history which confirms the explanation of the developments in our own time. In the age that preceded Waterloo, when Western Europe was enmeshed in a complicated system of tariff barriers, when each country was pursuing a policy of intense nationalism, inter-

vention and economic separatism, just as most of us have been doing for almost twenty years, Europe was ravaged by a series of long and destructive wars, and we did not escape either from participation or from their consequences.

The nineteenth century, in which relatively free trade was the dominant policy, presented a sharp contrast. If the one hundred years that spanned the period from Waterloo to the Marne was not a period of complete peace, at least men and women everywhere were not living under the shadow of destructive and universal wars. If it was not a period which provided as high a standard of living as we would like to have seen, at least it produced the highest standard of living the world had known. If it was not a period in which men were completely free, at least it was a period which was moving toward a complete liberation of man's inventive genius.

The first World War ushered out an age of tranquillity and ushered in a long period marked by efforts aimed at national self-sufficiency, the establishment of totalitarian states, large armies of unemployed until absorbed in the mobilization of national resources for military purposes, the threat of wars, and, at last, the actuality of war extending its area over increasingly large parts of the world's surface.

Now that war has come, even though we are not and do not become an active military participant, can we insulate ourselves against its consequences? Can we, for example, long stand the shock of further depreciation of currencies of important belligerent countries with which we must and can have traffic? Can we immunize ourselves against the effects of post-war liquidation, of the social pressures incident to demobilization, of the readjustments natural and inescapable in all post-war periods? Can we maintain our traditional forms and the substance of our American culture in a world which, unless we are prepared to play a part in reconstruction, may be cast in the mold of relatively extreme totalitarianism, using the totalitarian technique in world markets?

Much will depend on who wins the war. Much will depend on our willingness in our own interests to shoulder at least our share of the burdens of economic renovation.

There are many advocates of the system which they call free enterprise, sincere and honorable men, who would cure the evils of today with more protection, who insist that the only

way in which the American standard of living can be preserved is by adding more and more protective tariffs to those already in existence.

Hence it is relevant to ask what a standard of living is. Is it something which can be judged by a wage rate paid in one industry or group of industries? Is it to be measured in terms of earnings of circumscribed and limited groups in American society? Is not the standard of living rather to be measured by the degree of happiness and contentment, the amount of employment, the productivity, the volume of goods and services produced by our country? Are not the criteria by which we measure our standard of living employment and the production and distribution of wealth?

Can this be attained within the structure of democratic institutions and the framework of a system of free enterprise, even if they themselves can be preserved, without a stable, sound currency? And if it cannot, as I believe it cannot, then let the advocates of free enterprise pressing for higher protection demonstrate that this prerequisite, a stable currency, is compatible with that self-sufficiency toward which, barring Mr. Hull's gallant efforts, supported vigorously by the President, we have been rapidly moving. Let them show that what we now call the gold problem is a disease in itself, not merely the symptom of a disease. The burden of proof is on them. Let them prove that historical experience is wrong.

And now let us analyze the standard of living which these protectionist advocates of free enterprise would preserve. In part because of an economic nationalism initiated by us and imitated by others everywhere, we have a large volume of unemployed, maintained on a mean subsistence level only by huge withdrawals of the public moneys derived from a magnificent borrowing policy on the one hand and heavy exactions from the employed on the other. Is this the standard of living that the protectionist would protect?

The level of subsistence of those who work on the farms—the owner, the tenant and the laborer having lost their foreign markets through protection itself and the long list of disastrous consequences trailing in its wake—is maintained, just as the subsistence level of the unemployed is maintained, by public borrowing and the taking from some groups of an increasingly large part of their income and savings for the payment of

subsidies to other groups. Is this the standard of living, supported by artificial measures, condemned by the advocates of free enterprise as ruinous, which is to be protected? Is living in the shadow of war, with the large expenditures of public moneys it makes necessary for our national defense, the standard of living they would preserve?

Let those advocates of free enterprise who would subsidize one group by the imposition of exorbitant tariffs fly in the face of history and show that the self-sufficient national economy they would develop is compatible with the standard of living we would all welcome and with the self-same free enterprise to which they lend their support. Let them show that if one group is subsidized there can be withheld subsidies from other groups. Let them show that a country consisting of groups so subsidized by public authority is a country in which there can be preserved the form and substance of our civil liberties and the vital spirit of a self-reliant people. Let them show that countries unable to sell the products of their effort will not, if they can, obtain by force what they cannot obtain by the arts of peace and, hence, that self-sufficiency is not a soil in which the seeds of war take root.

In the light of experience, it can be suggested, if, indeed, it cannot be concluded, that a policy aimed at a progressive development of a self-sufficient economy is not compatible with the traditional American way of living, and that on the record of history fewer restrictions on and interferences with the movements of goods and services and the investment of capital offer a better promise of creating a tranquil, confident and happy world.

I would not infer that, under the pressure of war, we can move far in this direction. Nor would I minimize the difficulties of moving when the war is over. I would not imply, when peace comes, that we should then intemperately, excessively and unwisely remove all of the prohibitive barriers with which our economy has been circumscribed. But I do insist that by moving in the direction of lowering the barriers to the flow of goods and services, and by participating in the rebuilding of a stable international currency, we can only reconstruct the kind of a world in which the traditional forms of this Republic can be conserved.

There are some who hold the view that the vested interests are too deeply intrenched and the environment too unfavorable to reach out successfully toward this goal. I would remind them of the language of Adam Smith, written in 1776: "To expect, indeed, that the freedom of trade should ever be entirely restored in Great Britain, is as absurd as to expect that an Oceana or Utopia should ever be established in it. Not only the prejudices of the public, but what is much more unconquerable, the private interests of many individuals, irresistibly oppose it."

Yet within the compass of three quarters of a century complete free trade had become the settled policy of Great Britain and, for a short span, of the entire Western world. Can we not, if we will only take counsel of our courage, meet the issue as successfully as it was met more than one hundred years ago?

Remarks by the Chairman

Chairman Fraser: You are all cordially invited to the meeting which will begin in a few moments on the eighth floor, where Professor Sprague will tell you all about gold.

PART III

AMERICAN FINANCIAL POLICY UNDER THE WAR AND POST-WAR CONDITIONS

INTRODUCTION *

ELIOT WADSWORTH, *Presiding*
Chairman, American Section International Chamber of Commerce
Former Assistant Secretary, United States Treasury
Former President, Boston Chamber of Commerce

IT is my great honor to preside this afternoon at the meeting of The Academy of Political Science. We have three distinguished speakers who will talk on some very important subjects.

Those of you who heard the speeches at the luncheon meeting must realize that a good many illusions, under which the United States has been living in the last two or three generations, are now being severely tested. In fact, they are being subjected to an acid test, not only in our own prosperity but in our own minds, as to whether they have guided us along the right course. Just as we have to give up the good old tradition of Santa Claus, when we grow older, so we may have to get over a good many of the traditions in which we were brought up.

One of these traditions is the fact that the value of gold is inviolable. We know that gold has been a measure of value ever since the first year of the Christian era, and before that, and we have looked upon gold as something that we could forever rely upon. Now, as a result of the change in economic conditions in the world and the impact of science on the production of gold, which has suddenly, after twenty centuries, enabled us to produce the metal three or four or five times as fast as it was ever produced before, we find ourselves even worrying about gold and what is going to become of it.

* Opening remarks at the Third Session of the Semi-Annual Meeting.

So it is particularly appropriate that we have as one of the topics for the afternoon discussion, "The American Gold Problem and World Trade". We could not have a better expert, of greater experience and erudition, to expound the situation and explain it to us than Professor Oliver M. W. Sprague, Professor of Economics of Harvard University and former Economic Adviser to the Bank of England. I take great pleasure in introducing Professor Sprague!

THE AMERICAN GOLD PROBLEM AND WORLD TRADE

OLIVER M. W. SPRAGUE
Professor of Banking and Finance, Harvard University

THIS gold problem is full of complications and can hardly be handled adequately or comprehensively in any short period of time.

Perhaps I might better begin by mentioning a few aspects of the subject about which I suppose there will be no disagreement. The first of these is that we already have a stock of monetary gold in the United States far in excess of what is needed to support any desirable increase in the present volume of currency and credit. The second proposition is that this already superabundant gold stock is certain to be considerably enlarged during the course of the war, and presumably during the months of readjustment following its conclusion. Some billions of additional gold, we may reasonably presume, will come into the country during these next few years, thus increasing the aggregate monetary gold stock from the present eighteen billions to perhaps twenty-two or even twenty-five billions of dollars.

I think it may also be agreed that this additional amount of gold does not in and of itself greatly increase the danger of inflation. We could have inflation on a very solid gold foundation with our present stock of gold; consequently, adding a few billions of unwanted gold to the stock does not very greatly change the picture so far as the danger of inflation is concerned. Inflation does not result from the possession of a large stock of gold. Such a stock merely permits inflation on a gold foundation. In order to have inflation, you must have a condition of persistent demand for all available labor, and also for all available capital; and that is a situation which does not, unfortunately, appear to be in the offing at the present time. Therefore, I rule out inflation as a present danger arising out of the presence of this superabundant gold stock.

With twenty-five billions of gold rather than eighteen billions, it will be a more difficult job for our monetary authorities to check inflation when and if an inflationary tendency develops, but it can be done if the will to do it is present. Reserve requirements of the commercial banks can be increased, and the federal reserve banks can reduce the total holdings of earning assets, and, by these means, two or three billions of gold might be neutralized, but that would not turn the trick. It would not be enough with our present eighteen billions, much less with the prospective twenty to twenty-five billions.

It will be necessary, if inflationary tendencies develop, and the will to control them is here, for the Treasury to sterilize large amounts of gold by issuing additional government securities for the purpose of absorbing excess bank reserves. I assume that that will be the policy of our government. You can, therefore, see that I am not particularly disturbed, from a danger of inflation standpoint, by the continued inflow of gold; but there is another danger that has, perhaps, more reality. We, at present, hold something like two thirds of the total monetary gold stock of the world and will doubtless hold a still higher percentage before the present war is ended. It has been suggested in many quarters that the rest of the world may elect to conduct its monetary affairs without any gold whatever, and may be unwilling in the future to accept gold as an international means of making payment, leaving the United States with a great stock of gold which will be quite without value for any exchange purpose whatever.

Certainly, if gold were no longer to perform any monetary purpose, its value would decline to a very small fraction of the present price. Since there are few industrial uses for gold, that would develop merely because gold were available at twenty dollars an ounce, or ten dollars an ounce, or even one dollar an ounce, we might find ourselves possessed of twenty to twenty-five billions of gold having no appreciable exchange value. I think that this is a possible danger but I doubt very much whether it is a serious danger and I will venture to give you four reasons for this view, a view which to some of you may seem unduly optimistic.

In the first place, it should be borne in mind that there is a widespread interest in gold mining in various parts of the world — particularly in South Africa, Canada, Australia and

Russia. In addition to the producing areas directly concerned, there is also the influential financial interest in gold mining properties, particularly in Great Britain. A policy calculated to destroy the gold mining industry will, therefore, be certain to encounter strenuous opposition.

In the second place, and this is of very fundamental significance, monetary authorities in no country seem to be willing to acquire indefinitely large balances in the currencies of other countries. This is an attitude which, I believe, will persist in the future. Everyone concerned practically with monetary matters recognizes the need of some asset which will be readily accepted as a means of making settlements in foreign countries. In spite of the monetary disturbances of the last ten years, gold has held its position as an acceptable means of making settlements. Nothing has appeared to take its place—certainly not the paper pound and not even the paper dollar. Experience during the last few years does not indicate that any country that has enjoyed a favorable balance of payments has been unwilling to acquire gold. On the contrary, such countries as Switzerland, Belgium, Holland, Sweden, to say nothing of Great Britain, whenever payments have been favorable to them, have acquired gold. Now this, I think, is a condition which will presumably continue. I hope for a far more peaceful world, of course, than we have been living in in recent years—in fact, all my analysis is on the supposition of a more peaceful world. I should think, however, that it was unreasonable to anticipate such a complete community of interest and such complete confidence as to lead different countries to be prepared to build up indefinitely large balances in foreign countries. They will wish to take something which they feel reasonably certain will prove acceptable as a means of payment anywhere throughout the world. Gold has continued to hold that position and no other commodity has anything like that acceptability throughout the world, and I do not observe that the acceptability of gold has in the slightest degree diminished during these recent years of disordered currencies.

In the third place, in the absence of some acceptable means of making settlements, the universal adoption of bilateral compensatory trade and financial arrangements between countries would, in my judgment, probably be unavoidable. There has, of course, for other reasons, been a strong tendency in this

direction in recent years. It is certainly not a development calculated to increase the total volume of world trade. It has been a natural consequence of disordered economic and financial international relationships. If we are to move toward a more peaceful world, it may be presumed that bilateral trade arrangements will gradually disappear; but if gold should no longer be acceptable as a means of settlement, I very much fear that bilateral arrangements will become even more general than at present, and with little hope of their ultimate disappearance.

A fourth and final reason for my belief that gold will continue is related particularly to the functioning of a managed currency, and here I address myself to monetary theorists. Much criticism has been leveled at the gold standard on the ground that a rigid, fixed price for gold and rigid exchange rates frequently impede or prevent the adoption of desirable monetary policies, desirable within particular countries. That is the basis for the proposal that in the future we establish managed currencies. Now, it is not necessary that there be a permanent fixed price for gold and fixed exchange rates in order to secure the continued use of gold. Gold can play a part in a managed currency even though the currency system is one which permits a very considerable degree of elasticity, as regards the price of gold and as regards exchange rates.

I shall not undertake to discuss whether it will be desirable in the long run to establish an elastic price for gold, and elastic exchange rates. Merely for the purpose of this discussion, I shall assume that such a course is desirable; but then, I venture to suggest that without gold as a foundation or as a cushion, currencies cannot be controlled by the currency managers, that they will find in periods of stress that they are unable to give their currencies just the desired degree of elasticity that they think desirable from the point of view of their domestic situation.

In the entire absence of anything that the foreigner would be certainly willing to accept, I should imagine that, in a period of strain, speculation would develop against a currency, and in the course of time confidence in that currency would be so weakened that the currency managers would find that their currency was fluctuating within wider limits than in their opinion was desirable. The possession of a considerable amount

of gold would serve as a cushion, and give them the means, I believe, of adopting that currency policy which they happen to think is desirable, and in the absence of that cushion I should question their ability so to do. This seems to me to be a reasonable ground for my opinion that monetary authorities are likely to agree that gold should continue to play some part in the working of the international monetary mechanisms.

Now, let us turn to the question of the circumstances in which it is reasonable to anticipate a somewhat better distribution of gold than that which obtains at the present time, and particularly a better distribution of gold than the even more unsatisfactory distribution which may be anticipated at the close of the present war. Let me say, first, that I do not envisage any considerable reduction in the aggregate amount of gold held in the United States. If that figure is twenty-five billions of dollars at the end of the present war, it would be my guess that it will be twenty-five billions, ten or twenty years hence.

The best that we can look for in my judgment is that in the years following the war, if gold continues to hold its place as a part of the international monetary mechanism, the rest of the world will acquire future gold production. Now, the present annual output of gold is in the neighborhood of forty million ounces, and the total value is between twelve and fourteen hundred millions a year. If the rest of the world over a period of ten years were to acquire the present annual output, assuming it to be maintained as I think one may reasonably presume it will be, at the end of ten years the rest of the world would have ten to fifteen billions of gold (scattered among the various countries) more than it will have at the end of the war. That would give a not too bad distribution of the total gold stock as it then will be.

I do not anticipate an outflow of gold from the United States, because even to change the inflow involves so very considerable a change in the balance of payments of this country. We have received this gold partly because of an excess of exports over imports, and in part because of funds sent to this country either for investment or safekeeping. Had this war not occurred, it is at least possible that conditions would have so developed that a considerable part of the foreign funds that have come to this country in recent years would

have been withdrawn for employment at home; but, a major part of these funds will doubtless be expended in this country for the purchase of war products of one sort or another. Consequently, at the end of the war I think we may reasonably presume that not only shall we have more gold than now, but also that foreign investment and foreign funds in this country will have been quite materially reduced.

Whether there continues to be an inflow of additional funds from abroad, seeking investment and safekeeping, will depend, of course, upon conditions abroad relative to those here, obviously a matter over which we ourselves have no direct control. However, on the supposition of a satisfactory peace with a promise of a peaceful world, I should imagine that European funds would find employment at home for the work of reconstruction of their capital resources. There is, therefore, it seems to me, a fair probability that, in so far as gold has come to this country in recent years for investment reasons, the inflow may decline.

We now come to exports and imports. In this matter I am afraid that there is very, very little that the United States will do. It seems to me quite unlikely that the United States will change its tariff policy in a period of business inactivity in such fashion as to permit a large volume of goods to come in from the outside in competition with inactive American industries. That exports will shrink, owing to the inability of the rest of the world to find dollars, is perhaps a probability. We may get a more normal relationship between exports and imports through a shrinkage in exports; but I should not imagine that that would be a satisfactory solution from the point of view of the rest of the world; a mere reduction in exports, accompanied by a reduction of imports, does not look very satisfactory or promising.

I therefore wish to present what I believe to be the greatest single contribution which the United States can possibly make to a more satisfactory condition all around the world and so to a solution of the gold problem. It is a contribution that has no direct relationship to exports and imports. The United States is so large a country that we cannot expect a trade recovery on a broad front to be brought about here through an expansion of exports. We are already exporting an excessive amount relative to imports, and the billions of additional

exports that would be required really to bring about a broad recovery certainly cannot be developed beyond the temporary increase that may accompany this war.

If we are going to have a broad recovery in the United States we must produce more goods and services for home consumption. It was observed this morning that at one time we exported something like seven hundred thousand motor units to foreign countries. Well, you cannot imagine exporting a million and a half units to foreign countries; it would simply smother the foreign countries with cars when account is taken of their purchasing power, but an increase of a half a million cars in the United States per year is almost a normal kind of thing. We vary all the way from two million and a fraction to five.

This is a great consuming market of one hundred and forty millions of people, and full employment of labor and utilization of current savings in capital expansion must be directed primarily toward producing more goods and services for home consumption, whether that be in reconstruction of our railroads, improvement of our utilities, or in what seems to be the major possibility in this country—a transformation of housing conditions for the great mass of people.

The way to secure a broad recovery is to utilize our technological knowledge so that the man with the income of two thousand dollars shall, in the course of not too many years hence, be able to buy what the man with twenty-five hundred dollars is now able to buy, on the basis of the same general level of prices. If we advance in that direction, then we can really adjust our position to the rest of the world without any difficulty to ourselves, and to the great advantage of the rest of the world. For, given full employment, mainly concerned with the production of goods for home consumption, we should, as an incident of that widespread prosperity, buy more from abroad, and without inconveniencing any of our existing industrial groups. We should import more tea and coffee and cocoa and rubber and tin, and so on, in those circumstances. That is the basic means within our own control of bringing about a change which would lessen the inflow of gold, but until that comes about, I fancy that we shall continue to take in gold. Obviously we are not going to refuse to acquire gold when the refusal to do so would abruptly eliminate at least a

billion dollars' worth of purchasing power for our exported commodities. We could refuse to take in gold, but there would at once be an inevitable contraction in our exports. That we are unlikely to face in a period of widespread unemployment and business inactivity.

I feel that we shall probably continue to import gold until somehow or other we have succeeded in developing a sufficient demand for labor and capital in this country to yield widespread business activity, general prosperity and a higher standard of living, and when that time comes, the gold, I am confident, will cease to come in, and I am at the same time confident that the rest of the world, now one country and now another, as it develops a favorable balance of payments, will acquire some portion, large or small, of the current gold output of future years.

Remarks by the Chairman

Chairman Wadsworth: I think all of us here who have been worrying about the appraised value of that pile of gold that is accumulating in Fort Knox must take a good deal of encouragement from what we have heard from Professor Sprague in his estimate of the future of gold as a measure of values in this country and throughout the world.

One element discussed in part of Professor Sprague's general thesis on gold is the importance of foreign lending, and we are very fortunate to have the President of the Export-Import Bank of Washington, who will speak to us now on "Foreign Lending". I take great pleasure in introducing Mr. Warren Lee Pierson, President of the Export-Import Bank. Mr. Pierson!

FOREIGN LENDING AND THE EXPORT–IMPORT BANK

WARREN LEE PIERSON
President, Export-Import Bank of Washington

THE subject "Foreign Lending" presents so many implications and raises so many questions that I have concluded one would be brave indeed to attempt to present a brief paper on the subject which did much more than suggest the implications and, perhaps, add to the number of questions. Furthermore, I feel that in order to avoid any misunderstanding I should say that my remarks today, so far as they touch upon American governmental policies, are intended only to refer to those activities in the foreign investment field which are legally possible under existing legislation. I have no desire, nor would it serve any useful purpose, to discuss the political considerations which brought into existence certain laws restricting foreign lending such as the Johnson Act and the Neutrality Act. They were enacted to meet particular situations, and when these have changed, Congress can be trusted, we hope, to repeal or modify them if that appears to be in the national interest.

The past decade has provided us with many scholarly and factual treatises covering the whole field of international investment—prepared under both public and private auspices. Anyone who is interested can quickly turn to volumes which recite the experiences of leading creditor nations in seeking outlets abroad for surplus funds. The initial reaction of the layman to this page of financial history is likely to be that sending money abroad, whatever the country of origin, is pretty sorry business at best; and that a shrewd investor will squeeze his pennies a long time before turning them adrift in the stream of foreign commerce. As one distinguished group has said: "Debtor peoples regard international loans as a barrier to their future prosperity; creditor countries as the grave of their accumulated savings."

Disgruntled American holders (and we have a few of them) of defaulted foreign obligations will quickly appreciate the sentiment just expressed, but it is only fair to mention that the story of our own country leaves something to be desired. Investors in Europe have had unhappy experiences as a result of our railroad reorganizations; and, regrettably, several loans contracted by states after the Civil War were repudiated outright or scaled down substantially. As Miss Cleona Lewis has said in her excellent volume on *America's Stake in International Investments*, the record as applied to the present situation calls for a "sympathetic and understanding attitude on the part of the United States, the creditor of many defaulting nations, today."

People generally, and Americans particularly, are inclined to excesses of optimism and pessimism where investments are concerned. Between the bursting of the Mississippi Bubble in the eighteenth century and the enthusiasm with which we snapped at Latin-American bonds in the nineteen-twenties, little seems to have been learned. Or, to state it perhaps more accurately, the experience of investors of one generation or century is either unknown or overlooked by their descendants. One interesting phase of all this is the type of remedy we in the United States are prone to apply when it dawns on us that mistakes have been made. The tendency is to cure a bad finger by immediately cutting off the arm—rather than pausing long enough to diagnose the cause of the difficulty. Because certain foreign loans proved unwise, it does not necessarily follow that all such activities are either stupid or unsound.

The fact seems to be that in the final analysis, foreign investments have made constructive contributions to a troubled world. Without them there would now be little international trade as we understand the term, and the growth of the New World would have been greatly retarded. The construction of roads, the exploitation of mineral wealth, the building of cities and all the other activities in new countries required the expenditure of the savings of older societies; and with the overseas investment and the stimulation of foreign trade went another vital factor: the migration of population from the crowded centers of the Old World to the vacant fertile lands in the New. Only by large-scale, and often adventurous, lending could this country and many another have been de-

veloped. Certainly it is no exaggeration to say that what we are pleased to call "civilization" has been advanced much further by the utilization of savings of people at peace than by the weapons of military conquest.

Unfortunately, foreign loans have not always been confined to constructive purposes, but frequently have taken the form of advances to governments which used them for their military establishments or other nonproductive undertakings. On the whole, however, the development of complementary international trade has been so successful that it has come to be regarded as the normal type of international investment.

Long before the United States became a factor in the foreign lending field, the citizens of Great Britain, France and Germany had developed their respective lending "techniques". The British, on the whole, had much less direction from their government than did the French. The latter put great faith in governmental promises, whereas the British investors were usually more interested in having the borrower use the funds for productive purposes. Pre-war Germany's stake was much smaller but it is interesting to note that from the beginning she consciously endeavored through the use of surplus funds to develop herself industrially through enabling borrowers to trade with Germany. This effort did not usually interfere with Germany's political aims. France, on the other hand, was perhaps too prone, for her own good, to be satisfied with political rather than economic advantages.

Doubtless the individual investors in all of the countries named were more interested in the high return on their capital than in any real or imagined benefit to the state. Nevertheless, the state benefited, and it has been frequently said that through the development of foreign trade (made possible by foreign lending) the difficulties originally created by the Industrial Revolution were translated into a steady improvement in the standard of living.

Lending abroad takes many forms but these may all be broadly classified into (1) *direct investments*, and (2) *portfolio investments*. These two types have been subdivided into numerous categories which are doubtless helpful to those studying particular developments. For our present purposes, however, it is sufficient to say that direct investments include land, buildings and subsoil rights in foreign countries, and

shares of stock in foreign companies when acquired to influence or control their business operations. Portfolio investments include obligations of foreign governments, political subdivisions and corporations, and equities in foreign companies not held in large amounts or for the purposes of influencing management.

While American investments abroad even before World War I were substantial—having been estimated as something between $2,000,000,000 and $2,500,000,000—the unusual conditions brought about by the War caused both our direct and portfolio investments in other countries to increase tremendously. Simultaneously, foreign investments in the United States declined sharply. Estimates have been made which probably approximate the real figures, but it is enough to say that the net result was to change the United States from one of the world's largest debtor nations to one of the world's largest creditor nations.

Following, as it did, the impoverishment of Europe by the War, the pouring out of money by this country into international channels unquestionably averted immediate deflationary tendencies and economic collapse, but the bad news was merely postponed. Glad days they were. Unhappily the cold gray dawn arrived in due course; and with the accompanying headaches, foreign lending received a reputation which will not soon be lived down. The real shock was felt when, after wholesale defaults, standstill agreements and other similar incidents, we came suddenly to realize that the rôle of creditor left much to be desired. In fact, financial history will probably chalk up the nineteen-thirties as the Golden Decade for debtors!

International lending to be successful must be mutually beneficial to the borrower and the lender. While credits are an indispensable element in the development of raw material producing areas, the accumulated capital of industrial countries frequently surpasses domestic needs and must have foreign outlets if it is to be productive.

The most serious and ever-present threat to smoothly functioning foreign loan arrangements is the transfer problem which arises from a maladjustment of a country's balance of international payments. This occurs when the total sums received by a country from abroad are less than those which she

is called upon to send abroad. If all payments could be made in the same currency there would be no transfer problem, but most countries have their own medium of exchange—and payments to foreigners are usually required to be made in foreign currency. Stated in simple form, international payments require an exchange of currencies.

The failure of many people to understand this fact is largely responsible, I think, for much careless thinking upon the whole subject of foreign trade. I recall sitting next to a prominent lady at a Washington dinner while the Czechoslovakian trade agreement was being negotiated. She expressed keen indignation over the proposed slight lowering of duties on certain Czech goods. I suggested that this might be to our ultimate advantage since with the funds derived from merchandise sold here the Czechs could continue to buy some of our surplus raw cotton. "Nonsense," she said, "they can use money for cotton. Why must they send shoes?"

Transfer problems are especially troublesome in dealings between industrial and agricultural societies, because of the constantly fluctuating character and price of all raw material production and the frequent lack of diversity in commodities produced by raw material countries. The delicate exchange mechanism can be upset by a single bad harvest. Such a misfortune need cause no serious trouble if foreign capital loans are available, but in their absence recourse must be had to the reserves of foreign exchange and gold of the debtor country's banking system. Should these not exist, or be so depleted as to engender lack of confidence in the currency itself, the loans or other obligations due abroad are soon in a sorry position.

Agricultural countries have had the same experience as many business men—having discovered that when the need for financial assistance is greatest it is most difficult to obtain. High raw material prices stimulate capital imports; on the other hand, low prices for raw materials usually discourage capital imports. The private investor is seldom interested in bolstering a faltering foreign economy—even though the situation may appear to be a temporary one.

It is a fundamental condition of sound international finance that a country should borrow from abroad for capital development only if this development is of a type which is likely to improve its balance of payments in the future. Agricultural

countries prior to World War I fulfilled this condition because by borrowing for improved transportation or other developments, production increased. This is not invariably true today because new agricultural methods and the opening of new areas to cultivation have sometimes stimulated output beyond the capacity of foreign markets to absorb the commodities.

Even if borrowing abroad does not increase a country's capacity to export, the practice may still not be basically unsound for the reason that the borrowing may contribute to improve the future balance of payments, not by *increasing* exports but by *decreasing* imports. This does not aid the international exchange of goods, but it improves the ability to service foreign loans.

A strong tendency exists today in countries whose primary economy is agricultural to develop domestic industries. India and Canada are notable examples, but the trend is strongly in that direction in many South American countries. This drift is likely to continue and, with the return of more stable political conditions throughout the world, will probably even be supported by further protective measures. Here again we see that the replacement of imports of manufactured goods by home production contributes to improve the balance of international payments quite as effectively as an increase of exports.

There would appear to be no valid reason why the development of industries abroad should not be aided by direct investment or by loans, unless the utilization of such funds means direct competition with a development financed and owned by citizens of the country which is the source of the new funds. Especially is this true if the government is the lender. For example, the Export-Import Bank would not favor a loan to buy American equipment to be used to install an enterprise competing directly with a similar one already operating which is owned by our nationals. With this exception, such financing for productive industries seems both sound and proper, especially since experience has shown that gradual industrialization raises the general standard of living—resulting in a demand for new products—and improves the market for the seller.

A country which borrows from abroad is enabled thereby to sustain for the time being an excess of imports over exports, and an import surplus is in fact the normal condition of a country while borrowing largely from abroad. But a country

which borrows renders itself liable thereby to meet in future years the service charges (interest, sinking fund and dividends) on the sums borrowed. In order to meet these charges without recourse to fresh borrowing, it will eventually need an export surplus on the balance of commodity trade. For this reason it is important for both lender and borrower to insist that funds received from abroad are used in the manner most likely to contribute to the borrower's foreign exchange resources.

The foregoing will, I hope, serve as a sufficient background against which we can briefly consider present possibilities in the foreign lending field for the United States. With a constantly changing international picture — and especially one which is so disturbed—it is obviously not easy to lay down hard and fast rules. Even a twenty-four hour basis presents difficulties!

I wish to say, first, that I have no thought that indiscriminate foreign lending would be any wiser today—whether by private investors or by the government—than it proved to be in the nineteen-twenties.

My next observation is that it would be far better for the United States if all foreign lending were done by private investors, banking institutions or business concerns rather than by the government. However, unless and until private sources of capital are willing and able to carry on in this field, the government must take a hand if we are to protect traditional markets and assist those of our people who depend for a livelihood upon foreign outlets.

The realization that increasingly disturbed political conditions throughout the world made private businesses and individuals reluctant to accept the risks involved in the extension of foreign credits resulted in the creation by our government of the Export-Import Bank. There is not and has never been any intention to have the Bank do more than supplement private financial facilities. Until last year the only limitation upon funds the Bank could loan was the amount which the Reconstruction Finance Corporation would provide at the request of the Secretary of the Treasury and with the approval of the President. Nevertheless, in 1939 Congress placed a limit of $100,000,000 to its lending authority; the total loans outstanding at any one time theretofore had never exceeded

$60,000,000. The present Congress has authorized the Bank to lend up to $200,000,000, but with an annual national foreign trade well in excess of five billion dollars (exports and imports) the part which this institution can play is obviously a modest one.

In line with our general policy of supplementing rather than competing with the activities of private banks, we have made every possible effort to induce those institutions to participate with us in extending credits. Where this has seemed incompatible with their obligations to depositors, we have, nevertheless, in many instances authorized private banks to advance funds under our responsibility, and thus permit them to retain established relationships against the day when they may again wish to make such loans on their own account. The net result has been that our shippers, especially those handling cotton and other agricultural surpluses, have been able to retain valuable markets.

I would not wish to be understood as advocating the extension or even the maintenance of export markets if that were possible only through loans made without regard for their ultimate repayment. I say this because I know of no escape from the basic principle that foreign investments must ultimately be redeemed — or at least serviced — by the direct or indirect acceptance of the goods or services of the borrowing country.

Within certain limitations, however, it appears perfectly reasonable to provide credits, the proceeds of which create useful employment in the United States and at the same time assist the foreign exchange position of the purchasers' country either by increasing its salable exports or decreasing its imports. When the Export-Import Bank participates with an American manufacturer in extending credits to finance the sale of railroad, road-building or other basic equipment required for productive foreign developments, a mutually advantageous transaction results. The same is true when our facilities are used to provide American machinery and services for the installation of a foreign hydro-electric plant which reduces the need for imported fuels. Business of this character is especially valuable to the United States because it usually results in follow-up orders for replacements and extensions.

Mention has been made of the difficulties experienced by countries when extraordinary occurrences make it impossible to meet the normal requirements of their citizens for foreign currency. The Export-Import Bank has found that it can be of immense aid to our foreign traders by supplying credit lines to central banks of other countries in order to permit prompt payment for imports from the United States between major export seasons, after a crop failure, or following a severe decline in the price of an important export commodity. More recently, we sought to assist in maintaining our ordinary trade with the Scandinavian countries by furnishing small credits which were needed because of the effect of the present war upon their exchange positions. The shocking events of the past few hours may, of course, require us to cancel some of these commitments.

The credits authorized by the Bank to facilitate the exchange of goods between the United States and China is another example of the Bank's activities. Through financing furnished by the Bank our manufacturers have been able to some extent to keep American merchandise flowing to one of the world's greatest potential markets. In payment therefor the Chinese continue to supply us commodities such as wood, oil and tin of which we are always in need.

We are often called upon to decide the advisability and propriety of governmental credits to countries presently in default upon obligations to our private citizens. We have concluded that there is no "rule of thumb" answer to this problem. Each situation must be examined in the light of the facts and our own interests. If the country to which or in which the desired credits or loans are to be advanced has manifested a willingness to deal honorably with American interests already established and has evidenced the will to meet existing obligations to the extent of its ability, there appears no reason why conservative credits should not be made available—provided they are reasonably calculated to improve the borrowing country's foreign exchange position.

By the same token, a disregard for established American interests and the ability but lack of will to pay any portion of existing debts offer slight incentive for further investment in a country, either direct or portfolio.

Most if not all of the considerations which formerly provided the incentive for international investment still exist. Few countries have reached identical stages of economic development; and unless means are found whereby the creditor nations can — without incurring abnormal risks — once more employ their capital accumulations in productive foreign ventures, there is little reason to look forward to anything but a world divided into more or less self-sufficient units with their populations regimented beyond anything yet imagined. The almost universal desire for national self-sufficiency—which I fear the present war will not diminish—means that all peoples are becoming increasingly politically conscious. From this feeling flows a constant stream of new legislation affecting tariffs, labor relations and earnings. The "good old days" not only are unlikely to be seen again in the United States but are on the way out everywhere.

On the basis of the experience of the Export-Import Bank I am reluctant to believe that private international financial relationships will never again be resumed. I prefer to think that the conditions which are responsible for the disfavor in which foreign lending has fallen merely present a challenge to those whose business it is to grapple with this phase of modern life. Sooner or later the people of the world will tire of piling broken promise on broken promise. When this time arrives we may once more expect that obligations incurred will be more honored by their fulfillment than by their breach. May we not hope, therefore, that the resumption of intelligent lending—perhaps with some governmental participation—will one day contribute again to sounder trade and more cordial relations between nations.

Remarks by the Chairman

Chairman Wadsworth: May I announce that after the next speaker has concluded his remarks, there will be a period for debate, with a five minute limit, which will last a half hour, and by the orders of our dictator, Miss Warner, we will adjourn at five o'clock.

I now take great pleasure in introducing Mr. Percy W. Bidwell, Director of Studies, Council on Foreign Relations in New York City, who will speak to you on "The Effects of Belligerent Trade Restrictions on American Policy". Mr. Bidwell!

THE EFFECTS OF BELLIGERENT TRADE RESTRICTIONS ON AMERICAN POLICY

PERCY W. BIDWELL
Director of Studies, Council on Foreign Relations

A SPEAKER who comes ninth on a program like this reminds me of the child, youngest of nine, who is said to have remarked bitterly after Sunday dinner that he never had a chance to find out whether there was any other part of the chicken than the neck. I say that because the program is all interrelated. The question is whether I have anything left to talk about, except the neck!

Until a few days ago, military men occasionally referred to the present struggle in Europe as a "phoney war". Economists have never so regarded it. Certainly as far as foreign trade is concerned, it is the grimmest kind of struggle, conducted on a world-wide scale, with all the weapons available. Both sides are taking great risks, undertaking ventures which (although ultimately they may produce victory) for the present involve great sacrifice for their populations. Measures of economic warfare, such as the British blockade of German import and export trade, involve also interference with the trade of neutral countries to an extent which may disrupt or distort their economies. Neutral nations fear the results not only during the war period; they fear particularly the possible continuation of aggressive trade policies into the post-war era. The United States, the greatest of all neutrals, and next to the United Kingdom the world's greatest trading nation, is particularly concerned with the measures which the English and French took almost immediately at the outbreak of this war to control international trade.

In this paper, I propose (1) to describe briefly the principal methods of trade control; (2) to show what the effect has been upon our own import and export trade; and (3) to examine the various counter-measures which have been suggested as suitable for the United States.

First in time, and first in importance, as far as the United States is concerned, is the blockade of Germany and German controlled territory, applied first to imports into that country and after December 1939 to exports as well. This has meant cutting off markets for about $160 millions of United States exports and sources of $105 millions of imports.[1] With the extension of the combat area to Denmark and Norway, it appears that our entire trade with Scandinavia will be eliminated. Thus we can write off another $120 millions of exports and $80 millions of imports. The value of our trade interrupted by the blockade as it stands at present (April 1940) represents roughly 9 per cent of the total.

Next we may consider the restrictions which England and France have imposed on imports into their own countries. Import restrictions are an obvious means, when a country is at war, to protect the external value of the national currency by conserving supplies of foreign exchange, and to enforce economies on the civilian population. Both of these purposes are evident in the English and French restrictions. In addition, they are designed to switch purchases from markets such as the United States, where cash would be demanded, to markets in the sterling area where credit can be obtained or barter transactions utilized.

Other purposes apparent in British and French purchasing policy are: (1) the desire to assure to their home industries an adequate supply of raw materials at a reasonable price (this motive is apparent in the English agreement with Australia regarding purchases of wool); (2) to deprive Germany of supplies of materials from neutral sources, for example, the purchase of Swedish ore and Rumanian oil; (3) to make sure of a beneficent attitude on the part of neutrals or non-belligerents, for example, the purchase of tobacco from Turkey.

The mechanisms by which trade policies are implemented include import licenses, mass purchasing, bilateral trade agreements, the Anglo-French finanical and economic agreements, and a dual price system for sterling exchange.

Import trade is controlled through a system of licenses. No permits are issued for imports from foreign countries of luxury

[1] This computation is based on 1938 figures for our trade with Germany, Poland, Austria and Czechoslovakia. The figures for Scandinavia include the trade with Finland as well as Denmark, Norway and Sweden.

goods, nor of any goods that can be supplied from Empire sources. In issuing all permits, discretion may be used to direct purchases to countries where credit is obtainable, or where economic pressure may be used for political purposes. The government itself takes a hand in importing by mass purchases of colonial products. Thus it has bought up Australian and New Zealand wool and dairy products, Canadian lumber and West African cocoa.

Even before the war Americans thought Great Britain's agreements with Argentina regarding trade and payments forced the latter to discriminate against us. In October 1939 a new agreement provided that all sterling credits created in the Argentine by British purchases were to be used only for purchases or settlements in the United Kingdom. There are indications that this policy, which resembles the Nazi barter dealings, will be extended to other countries. Inevitably, they must result in narrowing the area in which multiangular trade can be conducted with free dollar exchange.

The announcement in November 1939 of an Anglo-French economic agreement, followed the next month by an even more inclusive financial agreement, aroused keen interest here. For the duration of the war, and for six months thereafter, the two countries will avoid competition in foreign purchases for government account, and will regulate their entire import trade according to a joint program. The pegging of the franc-pound exchange rate, combined with the prohibition of inter-country gold shipments, practically establishes a monetary and credit union. The beginnings of a customs union may be indicated by the mutual abolition of certain emergency tariff barriers. As far as this agreement foreshadows freer trade after the war relations within the great area bounded by the British and French empires, it is all to the good. But does it imply higher tariffs against the nations, like the United States, that remain outside? On what terms will outsiders be permitted to enter the "economic union"? These are questions of grave concern to the United States.

English exchange control affects principally American import trade. The characteristic feature of the control at present is the existence of two rates of exchange: the official rate, at present $4.03, and a free market rate, which is now about ten per cent below the official rate. According to a recent regula-

tion, certain exports from the British Empire, tin, rubber, furs, jute and jute manufactures, and whisky, must be paid for in belgas, guilders, Swiss francs or United States dollars, or in sterling acquired by the sale of those currencies at the official rate. The regulation is of particular importance to the United States; our imports of the enumerated commodities from British sources averaged in 1937 and 1938 about $300,000,000. For some of these commodities we are pretty much at the mercy of British policy; 75 per cent of our consumption of rubber and 85 per cent of our tin originate in British Malaya, and 100 per cent of our jute comes from India.

Naturally the British want to get as many dollars as possible for their raw materials, but, on the other hand, they are prevented from full exploitation of a monopoly position by the fear of alienating American opinion. Presumably $4.03 is somewhat above the "normal" level for the pound. To the extent which this is true, American buyers may be penalized, particularly since their demand for the enumerated goods is somewhat inelastic. But the dual rate system has possibilities also in another direction. By insisting that $300 millions of English goods be paid in dollars, a large part of the demand for free sterling is canceled, with consequent depression of its price in New York. Any increase in the number of basic commodities which must be paid for in dollars would tend to widen the spread between the official and the free rates. Such a result would favor British exporters of goods other than the enumerated commodities, at least temporarily; for every decline in the price of the pound, unless compensated by an equivalent increase in sterling prices, makes it easier for Americans to acquire British goods.

In certain characteristics, the English and French policies bear a striking resemblance to German commercial policy after 1934. Bilateral trading and multiple exchange rates are both familiar features of the Nazi system. They are also similar in their purposes. Both were designed to manage foreign trade so as to maximize national power. Both systems arose out of a desperate need for foreign exchange. The slogan, "Export or Die", is appropriate to both. This resemblance should not be surprising, since Germany in the years preceding the invasion of Poland was actually in a war economy.

Now that the English and French are at war, they naturally adopt commercial policies suited to a war economy.

The German policies elicited strong disapproval from the United States. We blacklisted Germany for failing to give our goods equal treatment in her markets. Germany thereupon stopped buying our cotton, shifting its purchases to Brazil, and made use of multiple exchange rates to force its goods into our markets. We retaliated with countervailing duties. Technically, there are only minor differences between their practices in 1934-1939, and the English and French practices of 1940. But the *trade situation* is entirely different.

For a number of years before we took action against Germany, trade with that country had been steadily declining, a situation for which German discriminatory policies were largely responsible. But now the war has stimulated our export trade with the Allies and with all the world. For the first six months of the war, the value of our exports was 33 per cent above the value recorded in 1938-39; if compared with 1937-38, the gain is less striking, but growth is indicated. Imports have increased more slowly than exports, but still there is no indication yet that belligerent restrictions have been injurious. Our industries are not being held up on their raw materials, and English manufactured goods certainly are not flooding our markets. Looking at the picture by countries, we find a gain of 15 per cent in exports to the United Kingdom and 117 per cent in exports to France. Large increases have taken place in our sales to Canada and Latin America. We have, in fact, displaced the United Kingdom as the principal supplier of foreign goods imported into Argentina.

So far, the Allied policies have not prevented a substantial gain in our total foreign trade. But they cannot be dismissed on that account as innocuous. We are concerned not only with changes in the total value of our exports, but also with the changes in the importance of the various commodities that make up the great stream of goods that pours out of our ports on its way to foreign lands.

War demand inevitably changes the character of our exports. The demand of the Allies in 1914-1918 brought about a great increase in our exports of cereals, meats and other farm products, and by stimulating agricultural production exercised a distorting effect on economic trends. Today, dis-

tortion is also present, but in the opposite direction. Our exports of manufactured goods have been stimulated; agricultural exports have been checked. The English, for example, are no longer buying fresh apples and pears from this country. The loss to our fruit growers is estimated at $10 to $15 millions annually. The effect of switching tobacco purchases from the United States to Turkey may prove much more serious. England has regularly purchased about one sixth of our total tobacco crop, spending here each year $65 to $70 millions. Up to 1939 our growers supplied between 75 and 80 per cent of all imports of tobacco into the United Kingdom; Turkey supplied two tenths of one per cent. But now Turkey, it is reported, has been guaranteed sales of 20,000,000 pounds annually, amounting to 10 per cent of British peace-time consumption. England also will probably increase its purchases of South African and Canadian tobaccos.

The prospective loss of a considerable share of the British market has already caused a substantial reduction in the acreage planted this year in Virginia and North Carolina. Thus the unbalance between agriculture and industry, which we have been experiencing since 1920 and which we have been at great expense to rectify, is being exaggerated by the war and by the import policies of England and France.

The reaction of American public opinion to the interferences of belligerent countries with our trade is now much less pronounced than it was twenty years ago. In the years intervening between two great wars, Americans have pretty thoroughly thrashed out the question of neutral rights, and seem to have concluded that it would be a mistake to insist upon them if we wish to keep out of war. Out of the controversy, there emerged the three Neutrality Acts, which seemed designed to avoid, if possible, the necessity of discussing with belligerents our rights to trade. Considered against this background, it is not difficult to understand why the British blockade of Germany accompanied by arbitrary procedures, such as contraband control and the examination of mail, have not aroused widespread public protest in this country.

Nor does the public in general seem to be upset by those features of Allied policy which affect adversely our trade with the United Kingdom and France, and indirectly our trade with neutrals. In 1916, Congress, fearing that trade restrictions

imposed by the belligerents might injure our commerce, authorized the President to impose penalty duties on goods coming from the offending countries, and even to exclude them from our ports. Although this Act is still on our statute books, no move has been made to apply it in the present situation. We have trade agreements with the United Kingdom, France and Canada, which are based on the principle of equality of treatment, but discrimination rather than equality seems to be the rule in war-time policies of these nations. It is true that the agreements contain clauses authorizing prohibitions and restrictions as war emergency measures, but there would seem to be difficulty in using them to justify policies which are actually discriminatory. Yet, we shall probably not denounce these agreements, for it should be noted that the Trade Agreements Act does not *compel* the President to withdraw the benefits of most favored nation treatment from countries which fail to give us such treatment in return. He is *permitted* to take such action when, in his opinion, the acts or policies of a foreign country tend to defeat the purposes of the law. Similarly, Section 338 of the Tariff Act of 1930, which is designed to check discriminatory action by foreign countries against American trade, authorizes the President to take retaliatory measures when he finds "that the public interest will be served thereby."

Countervailing duties might appear at first sight to constitute an exception to the general principle that retaliatory action is discretionary rather than imperative. Another section of the Act of 1930 (Sec. 303) makes it mandatory for the Secretary of the Treasury to impose additional duties on goods which have received a subsidy from a foreign country. But the mandatory character of the law is illusory, for Congress did not define " subsidy ". After long hesitation, the Treasury Department concluded that the German manipulation of multiple exchange rates amounted to paying a subsidy on exports to the United States. But it now seems clear that in making this decision a rather wide exercise of official discretion was involved.

Obviously, we have available a whole armory of retaliatory weapons, if we care to use them. But it is equally obvious that *we do not have to use them unless some important end is served thereby.*

Politically, retaliation seems impracticable. When so large a proportion of the American people want the Allies to win this war, it seems inconceivable that the Executive should find it in the public interest to start a trade war against them—especially since their restrictions have not been sufficient to check expansion in the value of total export and import trade. Moreover, retaliation might not be effective in accomplishing its objective. Instead of forcing the English and French to abandon their present policies, it might result in their buying even less of our farm products and more from Canada, Australia and the Argentine.

Two other courses are possible. We can sit tight, as far as external policy is concerned, and devote our attention to measures of domestic policy designed to ameliorate the disturbances in our economy which have been caused by the war, and which have been exaggerated by belligerent restrictions. We are already subsidizing various branches of agriculture; the subsidies can be extended if necessary. It is conceivable that the cost of such a policy might be recovered by special taxes on those branches of industry which are profiting most by wartime expansion.

A second alternative is to provide funds by which the Allies might buy some of our surplus farm products. Lack of dollar exchange, they complain, is the reason why they buy from Canada, Australia and the Argentine, rather than from us. By our cash-and-carry policy we have set up an artificial barrier to their buying here. Quite logically, they point out that we cannot have it both ways. We cannot deny them credit, in order to keep out of war, and at the same time hope to sell them products which they can get elsewhere "on tick".

But logic of this kind does not solve our problem. The question whether we are willing to relax present restrictions on lending goes considerably beyond calculations of our being involved in a war. Loans imply payment of interest and, eventual repayment of principal. Yet past experience seems to have taught us that we cannot expect any return unless we are willing to lower tariff barriers and accept a substantial increase in competitive as well as noncompetitive imports. Some of the speakers today have denied that there is any possibility of a genuine reduction in our tariff, either during or after the war. Mr. Douglas expressed the contrary view,

with which I am glad to associate myself. Substantial downward revision within the next twenty years I do not regard as at all impossible. But both he and I may be mistaken. If we are wrong, then the only sound policy is not to lend American money in any form to anyone. We ought to give it away, freely, "hoping for nothing again."

In this paper no detailed consideration can be given to the post-war situation. But it seems important to remark in conclusion that the attitude which we take today toward English and French policies should be determined not so much by their impact on our economy, here and now, as by the consideration of what they may mean in post-war years. Until 1939 England and France, the western European countries and Canada constituted a strong outpost of liberal trade policies in a rising sea of totalitarianism. In spite of minor lapses, all stood for equality of treatment in commercial relations. The United States still holds to that principle as indispensable in an orderly world. In a war emergency, the Allies have departed widely from their principles, and ours. Will they return when the war is over, or will they have become permanent converts to the policies of bilateralism and discrimination? It is this uncertainty regarding the future, rather than injury at present, which should constitute the greatest source of apprehension for Americans.

Remarks by the Chairman

Chairman Wadsworth: I want to apologize to the last speaker. That story was very well chosen but, as a matter of fact, we did get started late because of the luncheon and the radio time, which lasted to three o'clock, and that is really the reason why he feels like the ninth child in the family.

DISCUSSION: AMERICAN FINANCIAL POLICY UNDER THE WAR AND POST-WAR CONDITIONS

CHAIRMAN WADSWORTH: Now, we are going to have a few moments for very brief remarks.

MR. GEORGE CLARKE COX: I wish that I had the optimism of Professor Sprague. He evidently thinks there is only one way in which this war can end. Now, suppose that Germany wins. What becomes of our gold then? Germany is getting along without it now. Of course, they say she is having a bad time, but she is getting along. If she and Russia and all of Europe, including a conquered Britain and a conquered France, are what face us at the end of the war, I ask, what becomes of our gold? They do not have to take it. Germany makes everybody in her quarters take paper now, and she can make other people take paper if they are under her thumb. I shall not elaborate that.

On the other hand, suppose that Britain and France win? How is that going to distribute the gold? It is optimistic to suppose that those people, in a depleted state after the war, will have anything to buy gold with or that they will want gold. They will want more than anything else—goods. During the last war certain of the neutral nations refused Germany's gold, or said they did not want it; they said they wanted coal.

The third and last point I make is that gold cannot possibly be distributed unless there is a free gold market, and unless there is what we should call today, an unfavorable balance of trade. If we do not get that we will not only keep all the gold we have but we will get all the rest unless the Gold Reserve Act of 1934 is repealed.

CHAIRMAN WADSWORTH: Thank you, Mr. Cox. The debate is now open. Would anyone care to voice his opinion?

MR. H. SCHERBAK: May I ask the President of the Export-Import Bank whether it is necessary every time there is a surprise by Hitler or Japan that thousands of business men should lose their money because they do not receive any advance warning of the tensions and political disturbances, which never develop overnight.

I have wondered whether the economic service of the Bank is so sensitive that men who risk money in export can, through the Bank, benefit from the knowledge and experience of experts familiar with different parts of the world.

Chairman Wadsworth: The question is whether you are in a position to give information to exporters about situations abroad affecting their interests.

Mr. Pierson: My answer is that the Bank is not in a position to do it, inasmuch as its organization is small; and furthermore that type of facility is provided by other departments of the government and by private institutions. The present Bank staff consists of about fifteen people. We have no foreign service. In other words, we have no representatives in various countries. It is not particularly necessary, because most of our transactions are handled with American business men who come to see us or whom we go to see in this country.

Mr. Bernard Levmore: I would like to ask Professor Sprague about the fate of gold under new conditions. His discussion was based on the assumption that our private capitalist economy would continue after the war as it now is. Mr. Cox has suggested that after the war there may be an enlarged system of European autarchy, possibly under the Nazi cross. I would like to broaden that suggestion to include the possibility that European economies, at least, may organize themselves along either somewhat socialistic or semi-coöperative lines. What then would be the future of gold?

Professor Sprague: I should say that, if there are international dealings between different countries, some asset that is universally acceptable will be found quite convenient, and gold seems to me to be the one; so I suppose that, at least until this socialistic régime had settled down and functioned in good order, we would want some gold. But, if it ever does come and functions in good order, I think it would be a cheap price to pay for such an ideal condition—just to leave that gold in Kentucky.

Chairman Wadsworth: Is there anyone else who would like to ask a question?

Mr. Lin Lin: I would like to hear Mr. Pierson elaborate the actual operation of the loan to China. How does it stand now?

Mr. Pierson: The Chinese have serviced their loan remarkably well. During the first year, we disbursed some seventeen million

dollars of the twenty-five million dollar commitment. During that time the Chinese repaid interest, plus about three million dollars in principal. The service of the loan is entirely current.

CHAIRMAN WADSWORTH: We would be very glad to have another question or further discussion.

MR. GEORGE CLARKE COX: One word more, if I may. It is just this: I have rejoiced that nobody has mentioned the possibility of loaning gold. I hope that absurdity has been laid forever. You cannot loan gold. You can give it away, and then it will come right back to you.

CHAIRMAN WADSWORTH: We seem to do a great many things nowadays that a year ago we would have said we could not do.

MR. GEORGE CLARKE COX: I will modify that to say, if you do loan it you will be sorry!

CHAIRMAN WADSWORTH: Are there other questions? If not, I want to say to our three speakers that I think they have given us a most interesting appraisal of problems that are bothering us all, and that will probably bother us more before they bother us less.

If there are no other remarks, I will declare the meeting adjourned.